THE SIGNIFICANCE OF TRUSTEE INDEPENDENCE FOR THE VALIDITY AND ADMINISTRATION OF A TRUST

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DECLARATION

By submitting this dissertation electronically, I declare that the entirety of the work contained therein is my own, original work, that I am the authorship owner thereof (unless to the extent explicitly otherwise stated) and that I have not previously in its entirety or in part submitted it for obtaining any qualification.

Date: December 2020

ABSTRACT

The proper administration of the trust has proven to be fertile ground for academic study in South Africa. One aspect in particular, trustee independence, has contributed to divergent views in this respect. Of interest for this dissertation is the impact of trustee independence (or the absence thereof) on the validity and administration of the trust.

It is well established that trustees have a duty to act independently, but the theoretical basis for this duty of independence remains the subject of debate. In this dissertation, two competing propositions, identified herein as the “establishment” and “fiduciary” propositions are examined.

It is proposed that these propositions may be reconciled through the “independence duality model”, developed herein to provide a general theoretical basis for a trustee’s duty of independence.

The dissertation commences with an analysis of the history of, and what is considered the motive for, the development of the trust form. From this analysis, the duality in trustee independence emerges that serves as the basis for the model introduced herein.

The constituent parts of this model, the establishment proposition and fiduciary proposition, are further developed and it is proposed that this model serves as a sound basis to further explain the impact of a lack of trustee independence on the validity of a trust as well as the consequences that may follow where a trust, although valid, suffers from a lack of trustee independence.

The dissertation concludes with an application of the independence duality model to practical trust problems, thereby illustrating the utility of the independence duality model in determining contemporary difficulties encountered such as “sham trusts” and the abuse of the trust form.

OPSOMMING

Die behoorlike administrasie van trusts bly 'n vrugbare area vir verdere navorsing in Suid-Afrika. In hierdie verband het een aspek in besonder, naamlik 'n trustee se onafhanklikheidsplig, aanleiding gegee tot uiteenlopende sienings. Van belang vir hierdie proefskrif is die impak van 'n trustee se onafhanklikheid (of gebrek daaraan) op die geldigheid en administrasie van die trust.

Dit is geyk dat trustees 'n plig het om onafhanklik op te tree in die administrasie van die trust, maar die teoretiese basis vir hierdie plig bly onseker. In hierdie proefskrif word twee stellings wat poog om hierdie plig te verduidelik, naamlik die "geldigheid-stelling" en "fidusiêre-stelling, geïdentifiseer en verder ondersoek.

Daar word aan die hand gedoen dat hierdie twee stellings versoenbaar is deur die ontwikkeling van die "tweeledige-onafhanklikheidsmodel", 'n model onwikkel in hierdie proefskrif om die teoretiese basis van 'n trustee se plig om onafhanklikheid te verklaar.

Die proefskrif begin met 'n ondersoek na die geskiedkundige ontwikkeling, en beweegrede vir die ontstaan van die trustvorm. Hierdie ondersoek ontmasker 'n tweeledigheid in die konsep van trustee-onafhanklikheid wat die basis vorm vir die tweeledige-onafhanklikheidsmodel.

Die boublokke van hierdie model, die "geldigheid-stelling" en "fidusiêre-stelling", word verder ontwikkel en daar word voorgestel dat dit 'n verklaring bied vir die impak van 'n tekort aan trustee-onafhanklikheid op die geldigheid van 'n trust, asook die gevolge waar 'n trust, nietemin geldig, steeds gebuk gaan onder 'n tekort aan trustee-onafhanklikheid.

Die proefskrif sluit af deur die tweeledige-onafhanklikheidsmodel te toets aan die hand van verskeie, praktiese, trustprobleme. Daardeur word die waarde van hierdie model om kontemporêre trustvraagstukke, soos "skyn trusts" ("sham trusts") en misbruik van die trustvorm, te verklaar.

SOLI DEO GLORIA

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And lastly, my deepest possible gratitude is reserved for my wife, Ilené. Were it not for her love, unwavering support and selfless sacrifice amid the birth of our two children, and me carving out a practice at the Bar, this project would never have been completed.

TABLE OF ABBREVIATIONS

AFF	Attorneys Fidelity Fund
ALI	American Law Institute
IT	Information technology
REIT	Real estate investment trust
SCA	Supreme Court of Appeal
SCC	Supreme Court of Canada
TPCA	Trust Property Control Act 57 of 1988
UK	United Kingdom
USA	United States of America

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CHAPTER 1: IDENTIFICATION OF RESEARCH QUESTION AND DEMARCATION OF RESEARCH FIELD

1 1 Introduction

"A confidence reposed in some other…". This phrase, adopted by Garton to describe the conceptual starting point of the trust,[1] accurately emphasises, notwithstanding criticism,[2] the reliance placed on the character of another to ensure the proper administration of the trust.

The capacity of a trustee to do justice to this confidence, and the obligation to do so, form the basis of this research. As the discussion on the development of the trust in Chapter 2 reveals,[3] the trust grew from a societal need for an institution that permits one party (the founder) to transfer assets to another (the trustee) to manage for the benefit of yet another party (the beneficiary). However, this confidence placed in the integrity of the trustee to be faithful to his charge raises the potential for abuse. In this regard, Cameron observed that:

> "A bunch of crooked trustees can easily ransack a trust dedicated to philanthropic purposes. As happens. Honesty lies at the mercy of vigilant and scrupulous fellow trustees, unassisted by governmental oversight. So, too, with many private benefit trusts, where it is up to the trustees themselves, spurred, if they exist, by watchful beneficiaries, to see that the trust is properly administered".[4]

It is against this background of potential for abuse that three main principles of trust administration have crystallised, namely:[5]

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1 J Garton *Moffat's Trust Law* 6 ed (2015) 1. The phrase is from the sixteenth-century commentaries of Lord Chief Justice Coke, in reference to the "use", the ancestor of the modern trust. The full quote attributed to Lord Coke reads:
"A confidence reposed in some other, not issuing out of the land but as a thing collateral thereto, annexed in privity to the estate of the land, and to the person touching the land, for which *cestui que trust* has no remedy but by subpoena in the Chancery".

2 See FW Maitland *Equity, also, the Forms of Action at Common Law: Two Courses of Lectures* (1909) 42.

3 See part 2 2 in Chapter 2.

4 E Cameron as quoted from the preface of E Cameron, M de Waal & P Solomon *Honoré's South African Law of Trusts* 6 ed (2018) vi-vii.

5 305.

(i) that the trustee must give effect to the trust deed, properly interpreted, as far as lawful and effective;[6]

(ii) that the trustee must in performance of duties and the exercise of powers act "with the care, diligence and skill which can reasonably be expected of a person who manages the affairs of another";[7] and

(iii) that the trustee must, except as regards questions of law, exercise an independent discretion.[8]

It is this third principle, independent trustee discretion, which forms the focus of this research.

1 2 Research question

This research is primarily concerned with independence as one of the basic principles guiding trustees in their administration of the trust. More specifically, it examines the nature and theoretical basis of a trustee's duty of independence and considers whether it constitutes a fundamental requirement for the validity of a trust or derives from a fiduciary responsibility.

Therefore, the overarching research question that this dissertation considers is: what is the theoretical basis of a trustee's duty of independence?[9]

Following from the examination of this question is the development of a theoretical model to explain two different, but complementary, aspects of trustee independence. Ultimately it is argued that this model, and its constituent parts, (which can replace

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6 *Kalshoven v Kalshoven NO* 1966 3 SA 466 (R) 469A.

7 Section 9(1) of the Trust Property Control Act 57 of 1988 ("TPCA"). The Afrikaans text (which was signed into law) refers to "*die sorgsaamheid, ywer en kundigheid wat redelikerwys verwag kan word van 'n persoon wat die sake van 'n ander hanteer*". Section 9(2) of the Afrikaans text varies the wording, unlike the English text, to read "*die mate van sorg, kundigheid en vlyt soos in subartikel 1 vereis*".

8 *Ex Parte Bellinghan* 1936 CPD 515 517; *Ex Parte Knight* 1946 CPD 800; *Estate Gouws v Registrar of Deeds* 1947 4 SA 403 (T); *Badenhorst v Badenhorst* 2006 2 SA 255 (SCA) para 9.

9 A reference to a "theoretical" basis or discussion may be understood as a reference to the philosophical framework or justifications for a given approach to legal principles. However, in this dissertation the term should be understood as a discussion regarding the foundational framework for trustee independence.

existing models) may also be applied in the examination of other aspects of trust law, such as the phenomena of “sham” and “abuse of trust”.

1 3 Methodology

The research methodology followed in this dissertation is of a non-empirical and doctrinal nature. It is comprised primarily of analyses of case law and legislation, as well as a selection of domestic and international journal articles, theses and books. Although the focus of the research is on trusts in the South African context, reference is also made to various international works to inform the South African perspective where appropriate.

As appears from the discussion in Chapter 2, trusts from jurisdictions with a different approach to property law are by necessary implication conceptualised on a different theoretical basis.[10] In considering trusts in a comparative legal context, I have therefore adopted the approach followed by Honoré and recognised the division of the global legal systems into common-law, civil-law and mixed jurisdictions.[11] I am aware of criticism in characterising the legal families of the world in this manner[12] but remain of the view that this distinction is the most sensible and appropriate in the context of trusts.[13]

I draw from examples of three jurisdictions in examining the theoretical underpinnings of a trustee’s duty of independence. From common-law jurisdictions, material is primarily sourced from England. However, examples from the United

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10 See part 2 3 in Chapter 2.

11 T Honoré “On fitting trusts into civil law jurisdictions” (2008) *University of Oxford Legal Research Paper Series 27/2008* 3 <available at http://ssrn.com/abstract=1271079> (accessed 10-08-2019).

12 Gordley described the distinction between common law and civil law as “obsolete” – J Gordley “Common law und civil law: eine überholte unterscheiding” (1993) 1 *Zeitschrift für Europäisches Privaterecht* 498. In addition, one of the principal architects of one such classification, Kötz, has questioned whether the time has come to bid farewell to legal family classifications – H Kötz “Abschied von der rechtskreislehre?” (1998) 6 *Zeitschrift für Europäisches Privaterecht* 493. See also N Garoupa & M Pargendler “A law and economics perspective on legal families” (2014) 7 *Eur J Legal Studies* 33.

13 As discussed in Chapter 2, the civil-law and common-law trusts differ markedly in their theoretical underpinnings, especially in respect to the form of the rights enjoyed by the beneficiaries. See part 2 3 in Chapter 2.

States of America ("the USA"); Australia; New Zealand; Canada, and Jersey are also referenced.

Within the context of civil-law jurisdictions, reference is made to European continental authorities from Germany and Lichtenstein, as well as European Union legislation.

South Africa, as an example of a mixed jurisdiction, offers the bulk of the research material from this type of jurisdiction, both in terms of case law examined and the review of academic commentary, but material and examples from Scotland are also referenced.

1 4 Scope

Trusts are extraordinary legal institutions. The trust's most valuable characteristic has been identified as its versatility, which affords solutions to a myriad of legal problems – a proverbial legal wonder drug that solves "equally well family troubles, business difficulties, religious and charitable problems".[14] Apart from its "normal" use in, for example, the family and business contexts, trusts are also widely used to address vexing economic and social problems, such as charitable fundraising, black economic empowerment and off-shore investment. Unfortunately, the diverse use of trusts has also led to its widespread abuse.[15] Often trusts are trusts in name only with an essential principle of trust law, namely the independence of trustees, neglected.[16]

The early twentieth-century English historian and jurist, FW Maitland, was a particular admirer of the trust.[17] He in fact regarded the development of the trust as the "greatest and most distinctive achievement performed by Englishmen in the field of jurisprudence".[18]

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14 P Lepaulle "Civil law substitutes for trusts" (1927) 36 *Yale Law Journal* 1126.

15 See S Cohen "Investec trusts continue to warn of 'sham trusts'" (16-12-2006) *ItiNews* <http://www.itinews.co.za/companyview.aspx?companyid=22236&itemid=13E7229B-A559-422A-9AC9-DF2EA592C466> (accessed 24-07-2018).

16 *Land and Agricultural Bank of South Africa v Parker* 2005 2 SA 77 (SCA); *Tijmstra v Blunt-Mackenzie NO* 2002 1 SA 459 (T).

17 FW Maitland *Equity* 2 ed (1936) 23; FW Maitland *Selected Historical Essays* (1936) 129.

18 FW Maitland "The unincorporated body" (1902) *History of Economic Thought Papers*, *McMaster University Archive* <https://ideas.repec.org/p/hay/hetpap/maitland1902.html> (accessed 23-02-2019).

Garton suggests that it was not the ethical principles underlying the trust that excited Maitland, but rather its versatility and the dynamic nature thereof – evidenced through its development, "more in response to pragmatism than principle".[19] Garton also contends that this development in response to an ever-changing world shows no signs of slowing and while some branches of the law of trusts "have grown to full maturity … others have, as yet, scarcely sprouted, and a process of incremental development, usually gentle but at times more dramatic, is still occurring."[20] It is against the background of this continued development that he questions whether it is still appropriate to refer to the law of trusts in the singular, as opposed to "the laws of trusts in the plural".[21]

These questions simply emphasise that trust law is a rich and diverse branch of the law and that a limitation of the scope of this research is therefore essential.

This research is limited to the South African trust, with its civil-law theoretical underpinnings. While it cannot be discounted that the propositions advanced in this dissertation may also be applied to trusts found in other types of jurisdictions, it is not intended to offer a defensible theory on the theoretical justification of a trustee's duty of independence in that context.

Similarly, the scope of the research is limited to trusts in the strict sense.[22] While the positions of trustees in the strict sense may be compared to those of trustees in the wide sense, with inferences drawn from that branch of the law, the dissertation does not propose to justify the duty of independence of trustees in the wide sense.

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19 Garton *Moffat* 2.

20 3.

21 3.

22 Trustees in the wide sense must be distinguished from trustees in the strict sense. A trustee in the strict sense refers to those trustees of trusts defined in section 1 of the TPCA. Trustees that do not fall within this definition, but who nonetheless are entrusted with the affairs of others and consequently control property on behalf of others, have been described as falling within the ambit of trustees in the wide sense. It is self-evident that an examination of this second type of trust, despite not being subject to the provisions of the TPCA, can provide valuable perspectives on trusteeship in the strict or technical sense.

1 5 Examples

The practical impact of the themes examined in this research may be illustrated through examples. Each example represents a practical problem concerning the establishment and administration of a trust.

These examples relate to various aspects discussed thought this dissertation and are also drawn from case law discussed. The proposed outcome of each example will appear clearly from the discussion of the particular problem identified in the chapters that follow. In Chapter 7, I revisit these examples and offer an analysis of the, in my view, correct legal position against the background of the arguments developed in the preceding chapters.

1 5 1 Example 1

Assume an *inter vivos* trust where the founder does not intend to relinquish control over the trust assets. To achieve this end, he establishes a trust for the benefit of his children with three independent trustees and provides them with wide discretionary powers. However, he includes a provision in the trust deed to the effect that all decisions by the trustees are to be approved by the founder in order to be effective.

What is the effect of this provision and does this arrangement qualify as a trust?

1 5 2 Example 2

The next example may, for the sake of convenience, be divided into part “2a” and part “2b” as the facts are identical, save for one key distinction.

1 5 2 1 Example 2a

A founder establishes an *inter vivos* investment trust. The trust deed contains detailed and prescriptive provisions relating to the trustees. They are to invest the trust assets only in shares identified in an annexure to the trust deed, and only in the ratio set out therein.

The trust deed further requires that all proceeds from the investments be immediately re-invested in the same shares (and in accordance with the same ratio). It is expressly recorded that the trustees have no discretion in the investment of the trust assets and no amendment of the trust deed is permitted.

On the twenty-first anniversary of the trust, the trustees are to immediately liquidate the trust assets, pay the proceeds to the founder's surviving issue *per stirpes* and terminate the trust.

There is accordingly no requirement that the decisions of the trustees be approved by the founder, but the trustees' powers and duties are prescriptive in nature, with no discretion on their part. Does this arrangement qualify as a trust?

1 5 3 2 Example 2b

This example is identical to example 2a, with the only distinction being that the founder retains the power to amend the trust deed and, accordingly, the power of investment of the trustees.

What is the significance of this distinction? Does it compromise the validity of the trust?

1 5 3 Example 3

Also consider the following example. A founder establishes an *inter vivos* trust and appoints three independent trustees. The trustees are granted absolute discretion to invest the trust assets as they wish, to pay the income from the investments to nominated income beneficiaries and, upon their death, to allocate the balance to nominated capital beneficiaries.

To assist the trustees, the founder furnishes them with a letter of wishes proposing the manner of investments to be undertaken. The letter expressly records that the trustees are not bound by its content.

However, the trust deed contains a provision to the effect that the trustees' remuneration is to be determined by the founder on an annual basis, and that the founder may dismiss a trustee in writing.

During the currency of the trust, the founder regularly determines the trustees' annual remuneration in accordance with how closely they followed the suggestions in the letter of wishes. On one occasion and following from the trustees' refusal to follow any of the proposals in the letter of wishes, the founder dismisses the entire board of trustees and replaces them with three other persons.

Can it be said that this arrangement qualifies as a trust?

1 5 4 Example 4

A founder, a successful commercial farmer, donates the family farm and farming enterprise to a trust. He appoints five trustees, including himself, his wife, two sons and his accountant. The trustees are afforded unlimited discretion in the management of the trust assets and the beneficiaries are the founder and his family.

From the outset it is clear that the other trustees never question the management of the trust by the founder. Where resolutions are required, they all submit to his will in habitual deference and never bring an independent mind to bear upon the administration of the trust.

Does the conduct of the trustees imperil the existence of the trust?

1 5 5 Example 5

Consider the following alternative. The facts are identical to those of example 4, except that the trustees *do* bring an independent mind to bear upon the administration of the trust. At first, the trustees engage in robust debate surrounding the management of the trust assets and the enterprise as a whole, arriving at a decision (not always by consensus). With the passing of time, the founder's eldest son starts to play an increasingly prominent role in the management of the trust estate.

In time, the position develops where the remaining trustees simply permit the eldest son to manage the farm and farming enterprise as he sees fit and the remaining trustees come to simply submit to the will of the eldest son in habitual deference.

What is the effect of this gradual deterioration of trustee independence?

1 5 6 Example 6

A founder establishes a trust with the stated purpose of conducting a second-hand car sale business. The trustees are the founder, his business partner and an independent accountant. The trust deed requires that all the trustees act jointly in the administration of the trust. However, in reality, the accountant is never involved in the administration of the trust and the remaining trustees conduct the business without any reference to him. Effectively he is side-lined.

At one occasion the two trustees, purporting to act on behalf of the trust, enter into a sale agreement of all available trust stock with a third party. When market conditions change prior to delivery, it is apparent that the trust could sell the stock to another party at a premium. In order to profit from this state of affairs, the two trustees refuse to honour the first sale agreement, invoking in their defence that the third trustee was not a party thereto, rendering the sale agreement void.

What remedy, if any, does the third party to the first sale agreement have?

1 5 7 Example 7

A founder establishes various trusts to house his business, property portfolio, and investments. He is also the sole trustee and his children are the beneficiaries. He fails to ensure any functional separation between the various trusts and expenses are often shared. The maintenance of himself and his family is funded through the various trusts.

Long after the establishment of the trusts, the founder commences a business venture in his personal capacity. Upon the failure of this business venture, his personal creditors seek to execute against the trusts. Would these creditors enjoy any prospect of success?

1 6 Overview of constituent chapters

Including this introductory chapter and a conclusion, this dissertation is comprised of seven chapters.

This introductory chapter provides an overview of the material that is examined in the succeeding five chapters and identifies seven practical examples that are considered in the chapters that follow. These examples are revisited in the concluding chapter when the theoretical framework developed in the preceding chapters is applied to the examples identified herein.

Chapter 2 explores the trust from a historical perspective. It examines theories regarding its genesis and the development of the modern trust in South Africa. Principally, its purpose is to identify and discuss the core elements of a trust to enable an in-depth examination in the chapters that follow. It is intended in this chapter to illustrate the emphasis placed on the integrity of the trustee and the importance of the separation between control and benefit of the trust.

In so doing, Chapter 2 highlights the core elements of the trust and explores recurring themes such as the importance of the concept of the office of trusteeship and of leading judgments such as that in *Land and Agricultural Bank of South Africa v Parker*.[23]

Chapter 2, therefore, provides the necessary background against which issues of trustee independence may be examined in the chapters that follow.

Chapter 3 examines the theoretical basis for the principle of trustee independence. This chapter identifies and contextualises two theories (or propositions) for the requirement of trustee independence. As explained in that chapter these propositions, the establishment and fiduciary propositions,[24] appear *prima facie* mutually exclusive. The chapter nevertheless proceeds to examine the bases for these propositions and a model in terms of which they may be reconciled is developed. This model, the "independence duality model", forms the primary foundation upon which the propositions advanced in this dissertation are built. Significantly, the argument is advanced that the establishment and fiduciary propositions, independently, are insufficient to explain the requirement for trustee independence, but together provide a sound theoretical basis for the independence duality.

Chapters 4 and 5 develop the "independence duality model" through a further examination of its constituent parts – the establishment proposition (examined in Chapter 4) and the fiduciary proposition (examined in Chapter 5).

The central tenet of the establishment proposition is that the capacity for trustee independence is a pre-requisite for the establishment of a trust. In Chapter 4, the question is considered whether an arrangement where the trustees have no capacity to exercise any independent control over the trust assets can qualify as trust. In connection therewith, the question is also asked what type of control is relevant in determining the first question. In arriving at a proposition in this regard, the "control test" as developed and applied in the USA is examined and discussed.

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23 2005 2 SA 77 (SCA).

24 The terms "establishment proposition" and "fiduciary propositions" are entirely my own. However, the positions adopted by the principal advocates for each proposition discussed in this dissertation are in keeping with the descriptions as formulated herein and attributed to them.

Chapter 5 explores the fiduciary proposition. As explained in Chapter 3, this proposition holds that the requirement for trustees to bring an independent mind to bear upon the administration of the trust is rooted in the fiduciary duties of the trustee. Against this background, the ambit of a trustee's fiduciary duty is examined and the argument is advanced that it is this duty, flowing from the office of trusteeship, which requires a trustee to bring an independent mind to bear upon the administration of the trust. The consequences of a trustee's failure to live up to this obligation are also considered, for example where co-trustees uncritically accept the propositions of a dominant trustee.

Chapter 6 applies the independence duality model, and its constituent parts of the establishment and fiduciary propositions, in the context of sham and abuse of trust. In so doing, the establishment and fiduciary propositions developed in Chapters 3, 4 and 5 are applied to the contemporary difficulty of identifying and dealing with the abuse of the trust form. It is submitted that these propositions provide a sound theoretical framework against which sham and abuse may be measured and offer justification for either challenging the validity of the trust or disregarding the separate estate thereof.

The concluding chapter, Chapter 7, revisits the examples identified in this chapter and aims to provide an answer to the questions raised thereby with reference to the material examined in Chapters 3 to 6.

1 7 Conclusion

The analysis in Chapter 3 describes an academic controversy surrounding the theoretical basis of a trustee's duty to be, and remain, independent. In that chapter, I propose a model that reconciles the two primary theoretical propositions offered to explain this duty.

In the chapters that follow, these propositions are further examined and, for the reasons advanced in Chapter 6, I regard them as bringing significant clarity to contemporary trust difficulties.

This research departs from the premise that trustees have a duty to be independent in the administration of the trust, and that where the trust deed does not provide for the capacity for such independence; the existence of the trust is imperilled. In conjunction therewith, and to the extent that trustees do have the

capacity to be independent, the research investigates the consequences of a trustee's failure to honour this duty.

CHAPTER 2: THE DEFINITION, NATURE AND KEY FEATURES OF THE TRUST

2 1 Introduction

> "A trust is a legal institution in which a person, the trustee, subject to public supervision, holds or administers property separately from his or her own, for the benefit of another person or persons or for a charitable or other purpose".[1]

The above definition, with which Cameron et al open the introductory chapter of the sixth edition of their influential work on trusts, accurately encapsulates the essence of the trust institution and forms the basis from which its further development is to proceed.[2]

This chapter identifies and examines the core elements of a trust. In doing so, it explores the nature and key features of the trust institution from a historical perspective. An examination of the historical context from which the trust emerged serves to contextualise its core principles and also facilitates a meaningful discussion of its future development. Such a contextualisation is of particular significance for this study, which has as its aim the development of a theoretical framework explaining the requirement of trustee independence.

The purpose of this chapter is therefore partly introductory and partly aimed at placing readers from different disciplinary starting points – common-law lawyers, civil-law lawyers, and legal historians – on a common ground. Some readers may well therefore be familiar with parts of the material.

Central to this common ground is an appreciation of the core elements of the trust; the manner in which trusts, in both common-law and civil-law traditions,[3] provide

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1 E Cameron, M de Waal & P Solomon *Honoré's South African Law of Trusts* 6 ed (2018) 1.

2 See *Land and Agricultural Bank of South Africa v Parker* 2005 2 SA 77 (SCA).

3 De Waal points out that reference to the "common law" and the "civil law" as two distinct and separate bodies of law is not wholly uncontroversial. See MJ de Waal "In search of a model for the introduction of the trust into a civilian context" (2001) 12 *Stell LR* 63 n 3. For an introductory discussion of the different "legal families" of the world, see R Zweigert & H Kötz *Introduction to Comparative Law* 3 ed (1998) 63. For criticism of characterising the legal families of the world in this manner, see J Gordley "Common law und civil law: eine überholte unterscheiding" (1993) 1 *Zeitschrift für Europäisches Privaterecht* 498. One of the principal architects of such classification, Kötz, has also

limited liability without incorporation; and, most significantly, the principle that trusteeship is to be viewed not as a purely private-law obligation, but in reality constitutes a *quasi*-public "office".

What appears with increasing clarity as one progresses through this research, is that it is this last concept, trusteeship as an office, which is central to the explanation of many of the trust phenomena examined herein.

The chapter concludes with a discussion of *Land and Agricultural Bank of South Africa v Parker* ("*Land Bank v Parker")*[4] in which the Supreme Court of Appeal ("SCA") gave significant direction on the theoretical basis and future development of the trust in South Africa, and without which no discussion on trust law is complete.

2 2 Early development of the trust – trusts in the common law

Maitland famously declared that the trust was "the greatest and most distinctive achievement performed by Englishmen in the field of jurisprudence".[5] The history of the development of the common-law trust is interwoven with that of equity as it importantly came to mould itself around the concept of split ownership permitted in equity. Some authors have gone as far as to equate the history of trusts to that of equity.[6]

Therefore, the theoretical underpinning of the English trust (which is the ancestor of the South African trust) requires a brief elucidation of the development of "equity" as a legal concept in England.[7]

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questioned whether the time has come to bid farewell to legal family classifications – H Kötz "Abschied von der rechtskreislehre?" (1998) 6 *Zeitschrift für Europäisches Privaterecht* 493. See also N Garoupa & M Pargendler "A law and economics perspective on legal families" (2014) 7 *Eur J Legal Studies* 33. See also n 11 in Chapter 1.

4 2005 2 SA 77 (SCA).

5 FW Maitland "The unincorporated body" (1902) *History of Economic Thought Papers*, *McMaster University Archive* <https://ideas.repec.org/p/hay/hetpap/maitland1902.html> (accessed 23-02-2019).

6 F Sonneveldt "The trust – an introduction" in F Sonneveldt & HL van Mens (eds) *The Trust – Bridge or Abyss between Common and Civil Law Jurisdictions?* (1992) 2.

7 E Cameron as quoted from the preface of E Cameron, M de Waal & P Solomon *Honoré's South African Law of Trusts* 6 ed (2018) 26.

2 2 1 The development of "equity"

To a South African lawyer, the term "equity" may connote a principle of justice or fairness, and to act "equitably" would be synonymous with acting "fairly". However, in the context of English law, "equity" describes a particular body of law, with distinct rights and remedies that developed independently from the rest of the common law.[8]

The Oxford Dictionary of Law defines "equity" as:

> *"n*. 1. That part of English law originally administered by the Lord Chancellor and later by the Court of Chancery, as distinct from that administered by the courts of common law."[9]

Equity can be traced back to 1066 and the Norman Conquest of Britain by William the Conqueror. Prior to this date, there was no developed government or judiciary operating throughout England and instead society was organised by a system of "custom" applied by diverse decision-making bodies ranging from the King's Council to village meetings.[10]

Custom varied according to geographical location and, after the Norman Conquest, the Normans introduced a new system of law that was meant to be *common* to the entire realm, rather than the uneven patchwork of tribal customs that was applied up to that point.[11]

According to Jenks, it is wrong to assume that the new common law was in effect Norman law transplanted.[12] As part of an apparent battle for the hearts and minds of his new subjects, William the Conqueror promised to respect the "law of the land" and the customs that governed English society. However, the fragmented nature of the system appeared untenable to the highly organised Normans. Jenks explains that:

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8 PH Pettit *Equity and the Law of Trusts* 10 ed (2009) 3. For a history of the development of equity see also: RA Pearce & W Barr *Pearce & Stevens' Trusts and Equitable Obligations* 6 ed (2015) 12 and A Hudson *Equity and Trusts* 9 ed (2017) 12.

9 EA Martin *The Oxford Dictionary of Law* 5 ed (2002) 178.

10 Pearce & Barr *Trusts* 4.

11 Hudson *Equity* 13.

12 E Jenks *A Short History of English Law from the Earliest Times to the End of the Year 1911* (1924) 17.

> "Whatever else the Norman Conquest may or may not have done, it made the old haphazard state of legal affairs forever impossible. The natural desire of the conquerors to make the most of their new acquisition, the exceptional administrative and clerkly skill of the Normans, the introduction of Continental politics, the rapid growth of the country in wealth and civilization, soon proved the old customs to be inadequate. For some time, no one could tell what was going to take their place. In the end, there emerged a new national law; some of it based on immemorial native usage, some of it unconsciously imported from foreign literature, not a little imposed by the sheer command of a new and immensely stronger central government. The precise share attributable to each of these sources will, probably, never be ascertained."[13]

The focus of this new common law was the *Curia Regis*, or King's Court, reinforcing the notion that justice was the prerogative of the Crown. During the 1180's, Sir Ranulf de Glanville wrote a treatise on the workings of the King's Court and produced "a coherent system of English law deriving ultimate authority from the King".[14]

In its early development, common-law judges had a wide discretion to do justice, and there was little need for a jurisdiction to remedy defects in the common law.[15] The discretion common-law judges enjoyed to serve justice was especially pronounced in the informal procedure characterised by informal "plaints" or "bills", also referred to as "*querelae*"[16] (as opposed to proceedings commenced by writ), in the General Eyre.[17] The General Eyre was a form of circuit court that visited various counties between the twelfth and thirteenth centuries in order to administer justice. These justices have been described as "the first men to begin to forge a law common to all England".[18] Visits by the justices of the General Eyre decreased during the thirteenth century as the functions performed by those courts were increasingly undertaken by other institutions. In 1294, on the eve of the outbreak of

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13 17.

14 Baker JH *An Introduction to English Legal History* 2 ed (1979) 12, quoted by Pearce & Barr *Trusts* 13.

15 Pettit *Equity* 2.

16 From "*querela*" – a "complaint"; DA Simpson *Cassell's New Latin-English English-Latin Dictionary* (1973) 495. For a general discussion of the nature of the plaints and bills, see C Burt "The demise of the General Eyre in the reign of Edward I" (2005) 120 *The English Historical Review* 1.

17 Pettit *Equity* 2.

18 WT Reedy "The origins of the General Eyre in the reign of Henry I" (1966) 41 *Speculum* 688 688.

war with France, the General Eyre was suspended indefinitely, never to be revived on a national scale again.[19]

The Courts of Common Law, Common Pleas, Exchequer and King's Bench had by 1234 evolved from the *Curia Regis* to become the *de facto* administrators of justice.[20] In these courts, a plaintiff seeking to commence action needed to obtain a royal writ authorising the commencement of proceedings, as opposed to commencing proceedings by *querelae*. Writs were purchased from the King's Chancery and plaintiffs could procure new writs in order to redress novel legal problems leading to further development of the common law. The development of the common law in this manner was brought to an abrupt halt in 1258 with the proclamation of The Provisions of Oxford, which prevented the issue of new writs without the express permission of the King's Council. The effect of these provisions was to confine plaintiffs to only bringing cases within the terms of the existing writs.[21] In so doing, the common law's ability to develop effective redress for new types of cases was effectively hamstrung, resulting in it becoming stultified and inflexible.[22] It was this "straightjacketing of the common law"[23] and the, as yet unexplained, disappearance of plaints without writ that gave rise to equity as a branch of the law.[24]

Notwithstanding the fact that remedies available under common law were confined to pre-existing writs, and that the common-law courts had become separate from the *Curia Regis*, it was still recognised that a *residuum* of justice vested in the King. Accordingly, any person who failed to obtain justice in the common-law courts could approach the King for a remedy.[25] These remedies were based on what appeared to be equitable in the prevailing circumstances of each case. From early on the authority to provide equitable remedies where the common law failed was

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19 Attempts to revive the General Eyre were considered and a commission, the Trailbaston commission, was established to assist in the re-establishment of the General Eyre. See Burt (2005) *The English Historical Review* 12. It is generally recognised that attempts at re-establishment were unsuccessful and that by the fourteenth century the General Eyre had ceased to be held. See, Pettit *Equity* 3.

20 Pearce & Barr *Trusts* 4.

21 4.

22 Pettit *Equity* 3.

23 3.

24 Pearce & Barr *Trusts* 4.

25 Pettit *Equity* 1.

conferred upon the Lord Chancellor.[26] As the practice of petitioning the Chancellor became more frequent, the Chancellor and his office, the Chancery, inevitably acquired the characteristics of a court.[27]

The Chancellor dealt with cases on a more flexible basis and was more concerned with a fair result than with the rigid principles of law. The law pronounced by the Chancellor came to be known as "equity" and was intended to mitigate "the rigour of the common law".[28] Hudson explains that the courts of equity did not necessarily concern themselves with strict legal rules, but instead focussed on inquiring into the defendant's conscience. He cites the example of Chief Justice Fortescue who, in 1452, declared that: "We are to argue conscience here, not the law".[29] This resulted in two parallel judicial systems administered by separate courts and an inevitable struggle for dominance.

The Lord Chancellor's flexible approach caused concern among judges of the common-law courts. These concerns led Selden to proclaim that:

> "Equity is a roguish thing. For [common] law we have a measure … equity is [decided] according to the conscience of him that is Chancellor, and as that is longer or narrower, so is equity. 'Tiss all one as if they should make the standard for the measure a Chancellor's foot."[30]

Selden's joke mirrored contemporary criticism that the measure of equity depended on the identity of the Lord Chancellor. Hudson explains this variable approach adopted by different Lord Chancellors on the basis that they were, first and foremost, politicians:

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26 Petitions addressed to the "Chancellor and the Council" are to be found as early as the reign of Edward I and accordingly coincide with the demise of the General Eyre – see Pettit *Equity* 1.

27 2.

28 *Earl of Oxford's Case* (1615) 1 Ch Rep 1 per Lord Ellesmere LC: "to soften and mollify the extremity of the law"; *Lord Dudley v Lady Dudley* (1705) Prec Ch 241 244 per Lord Cowper: "Equity is no part of the law, but a moral virtue which qualifies, moderates and reforms the rigour, hardness and edge of the law".

29 Hudson *Equity* 13. Hudson explains that he meant that the role of courts of equity at the time was to reach a morally correct result, without being concerned with precedent.

30 F Pollock *Table Talk of John Selden* (1927), quoted by Hudson *Equity* 14.

> "In truth, before Robert Walpole became the first Prime Minister in 1741, it was the Lord Chancellor who would have been considered the 'prime minister' to the Crown."[31]

With time, general equitable principles emerged and its jurisdiction, once flexible, had ossified into a body of precedent with fixed principles.[32] The development of equity as a parallel judicial system intensified the friction with proponents of the common-law judicial system. This struggle came to a head during the reign of James I when the primacy of equity was confirmed. During this time it had become a feature of chancery courts to order so-called "common injunctions" ordering a party to a common-law dispute to either restrain his action, or to prevent the enforcement of a judgment obtained though the common-law courts. Refusal to obey these injunctions was regarded as contempt of court, attracting the threat of imprisonment.[33]

The "common injunctions" therefore represented a real threat to the jurisdiction of the common-law courts, which adopted the approach that imprisonment for disobedience thereof was unlawful and ordered the release of those affected. The ensuing jurisdictional war was settled in 1616, when James I issued an order in favour of the chancery courts and the common injunctions.

This order signalled the irreversible ascendancy of equity over common law and, notwithstanding attempts to reverse the trend,[34] the superiority of the chancery courts was well established by the end of the seventeenth century.[35]

The Judicature Acts of 1873 and 1875 reaffirmed the primacy of equity. These acts effected a restructuring of the English court system in terms of which the common-law courts and chancery courts were consolidated and merged to form a single "Supreme Court of Judicature". A central feature of the reform was that all the courts of the Supreme Court of Judicature, irrespective of their history, were to have both common-law and equity jurisdiction.[36] The Judicature Acts not only did away

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31 Hudson *Equity* 14.

32 Martin *Dictionary of Law* 179.

33 Pearce & Barr *Trusts* 6.

34 For example, a bill introduced in the House of Lords in 1690 to restrain the courts of equity from exercising jurisdiction over disputes for which a remedy in common law was available was defeated. See Pearce & Barr *Trusts* 7 n 9.

35 7.

36 Hudson *Equity* 15.

with the power to grant common injunctions, but also affirmed the supremacy of equity over the common law. In this regard, section 25 of the Supreme Court of Judicature Act of 1873 provided that:

> "Generally, in all matters not hereinbefore particularly mentioned in which there is any conflict or variance between the rules of equity and the rules of common law with reference to the same matter, the rules of equity shall prevail."[37]

In that manner, equity was enshrined as "regulating the conscience of a person where the common law might otherwise allow that person to act unconscionably".[38]

This principle was re-asserted in *Westdeutsche Landesbank Girozentrale v Islington LBC*[39] where Lord Browne-Wilkinson held that:

> "Equity operates on the conscience of the owner of the legal interest. In the case of a trust, the conscience of the legal owner requires him to carry out the purposes for which the property was vested in him (express or implied trust) or which the law imposes on him by reason of his unconscionable conduct (constructive trusts)."[40]

It is against this backdrop of equity as the conscience of a defendant and counterweight to the rigour of the common law that the birth of the trust institution in England must be viewed.

2 2 2 The development of the "use"

Understanding the development of the trust requires a basic understanding of the feudal system of landowning that prevailed in England during the medieval period.

Since all land was owned by the King, individuals were granted "tenure" over land by a landlord, who in turn would enjoy tenure from another landlord. This gave rise to a tenurial system of tiered landholding – a pyramid of tenure with the King at its apex.[41] This system resulted in reciprocal obligations between landlord and tenant. For example, a tenant would be required to perform some service for or on behalf of

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37 16.

38 9.

39 [1996] 2 All ER 961.

40 988.

41 K Gray & SF Gray *Elements of Land Law* 5 ed (2009) 65.

his lord, who in turn owed the tenant enjoyment of the tenement as long as the service was maintained.[42]

While tenure determined the terms under which land was held, the parallel "doctrine of estates" determined the duration for which a grant of tenure was to last.[43] An estate in fee simple, for example, was a grant of tenure in perpetuity, [44] and within the feudal structure the right to tenure of land in fee simple was tantamount to absolute ownership. Akkermans explains as follows:

> "This most extensive entitlement [in the estate in fee simple] is meant both in time and space. A holder of a fee simple is allowed to exercise his right to possession forever and, in principle, exclusively. The term 'fee' refers to the feudal grant, which is the origin of this estate. The term 'simple' refers to the fact that the estate will pass to the heirs of the holder, not of any particular category, as was the case with a fee tail or estate in tail."[45]

Upon the death of a tenant, the person who succeeded to the tenure (and acceded to the relevant position on the feudal ladder) was required to make payment to the direct landlord. These inheritance taxes, termed "feudal incidents", provided a significant source of revenue for the feudal system and, ultimately, for the Crown.

It is within this feudal context of landholding that the trust developed, but the precise origin of the trust remains unclear.[46]

What is clear is that the trust developed from the earlier "use"; an arrangement in terms of which property was transferred to a person, for the use of another. Hudson points to an account that places the source of the use in the Middle East and the emergence of the "*waqf*". The latter is a device used within Muslim communities to provide for property to be held by one family member for the benefit of other family

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42 These services may have included agricultural services, religious services, or the provision of military support.

43 See Pearce & Barr *Trusts* 14 n 36 and the reference to *Walsingham's Case* (1579) 2 Plowd 547 555:
"the land itself is one thing, and an estate in the land is another thing, for an estate in the land is a time in the land, or land for a time, and there are diversities of estates, which are not more than diversities of time …"

44 Pearce & Barr *Trusts* 14. An estate in fee simple is to be distinguished from a "fee tail" (or "entailed interests") which was only meant to endure for as long as the grantee had lineal descendants, and a "life interest", which was to last only for the grantee's lifetime.

45 B Akkermans *The Principle of Numerus Clausus in European Property Law* (2008) 346.

46 Hudson *Equity* 37.

members.[47] The *wafq* is an unincorporated charitable trust and was developed to accommodate Islamic restrictions on the passage of property to heirs.[48]

It has been suggested that in the twelfth century, Christian noblemen may have encountered the *waqf* while away on crusades[49] and brought the idea back to Europe.[50] Upon returning to the front, such a knight would transfer his land to a trusted friend who would administer the land in his absence.[51] The instruction was usually to transfer the land back upon the knight's return, and failing such return, to transfer the land on to an identified beneficiary.[52]

There are, however, other theories for the development of the use.[53]

The first is that the use developed from the Roman *fideicommissum*, introduced to ameliorate the inflexibility of the *ius civile*, which prohibited certain persons from being named beneficiaries under a will.[54] Through the *fideicommissum*, a testator could entrust property to another to be conveyed to a person that would otherwise have been appointed as a legatee, were it not for the prohibition. Albertus points to the example where a testator would, in view of a prohibition on making bequests to non-Romans, bequeath property to an individual who was capable of receiving it, with the request that the property be delivered to the named beneficiary, that is, the non-Roman.[55] In this manner, property could be made over to one person, who would be obliged to deliver it to the ultimate beneficiary.

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47 Hudson *Equity* 38. See also H Lim "The waqf in trust" in S Scott-Hunt & H Lim (eds) *Feminist Perspectives on Equity and Trusts* (2001) 47.

48 L Albertus "Comparing the *waqf* and the South African trust" (2014) *Acta Juridica* 268. Cameron et al *Honoré* 19, n 122.

49 A controversial term, but one that historians nevertheless still use to describe this particular conflict. See J Theron & E Oliver "Changing perspectives on the Crusades" (2018) 74 *Herv Teol Stud* 12.

50 J Garton *Moffat's Trust Law* 6 ed (2015) 36. See also A Avini "The origins of the modern English trust revisited" (1996) 70 *Tul LR* 1139; S Herman "*Utilitas ecclesiae*: the Canonical conception of the trust" (1996) 70 *Tul LR* 2239.

51 MM Corbett "Trust law in the 90s: challenges and change" (1993) 56 *THRHR* 262.

52 MJ de Waal "The core elements of the trust: Aspects of the English, Scottish and South African trusts compared" (2000) 117 *SALJ* 548 553.

53 For an insightful discussion on the differing theories for the development of the use, see F du Toit, B Smith & A van der Linde *Fundamentals of South African Trust Law* (2019) 17.

54 18.

55 Albertus (2014) *Acta Juridica* 271.

Another theory is that the use developed from the *Treuhand,* a Germanic institution of the *Lex Salica*, the civil code of the Salian Franks dating from the fifth century.[56] The *Treuhand* permitted a third party, the *salman* (or "*saalman*"), to act as an intermediary in property transfers to third party beneficiaries. In terms thereof, property was made over to the *salman*, with the obligation to deliver it to a designated beneficiary upon the death of the initial transferor.[57] This theory is buoyed by proof that elements of Salic law were introduced into England through the Norman conquests.[58]

This also appears to be the theory preferred by the South African Appellate Division, which declared in *Braun v Blann & Botha NNO* ("*Braun*")[59] that:

> "Uses and trusts were introduced into England shortly after the Norman conquest. The trust was developed by the English Court of Chancery from the Germanic Salman or Treuhand institution rather than from the Roman *fideicommissum* or other juridical institutions of Roman law."[60]

A further theory proposes that the use developed from a combination of Roman and German influences. In this sense, it has been suggested that the word "use" derives from the Latin word "*opus*". "*Opus*" was encountered in England during the ninth century and can be traced to the records of early Germanic tribes such as the Franks and the Lombards.[61] It has been proposed that medieval Franciscan friars employed the phrase "*ad opus*" to describe an arrangement which permitted them the use of property held by others, eventually culminating in the trust.[62]

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56 Du Toit et al *Fundamentals* 18.

57 18.

58 18.

59 1984 2 SA 850 (A).

60 859A.

61 Du Toit et al *Fundamentals* 18.

62 Albertus (2014) *Acta Juridica* 273.

A further theory still is that the use has no continental ancestor and was simply an invention of the English courts of chancery to give effect to the maxim that "equity acts on the conscience" and is designed to temper the rigours of the common law.[63]

The debate on whether the use descends from the Islamic *waqf*, the Roman *fideicommissum*, the Germanic *Treuhand*, or was an original development of English equity, may well remain unsettled. However, perhaps the value of this debate lies not in the ultimate unmasking of the use's forefathers, but in the illustration that the desire to develop an institution "to protect the weak and to safeguard the interests of those who are absent"[64] is a universal human need that transcends cultural divisions.

2 2 3 From "use" to "trust"

Whatever the historical roots of the use, it found expression in the chancery courts. In its most simple form, it was a structure in terms of which X would convey land to Y "for the use" of Z. In this example, Y was termed the "*feoffee*"[65] (or "*feoffee* to use") and Z the "*cestui que use*".[66] The common law courts did not recognise this "use" of land and regarded the *feoffee*, in whom the legal title was vested, as the absolute owner.[67]

However, the chancery courts, rooted in equity, were prepared to enforce the use, requiring the *feoffee* to administer the property vested in him for the benefit of the *cestui que use*. The effect of this recognition was that, while Y became the owner of the land, he was compelled to apply it for the benefit of Z and was prevented from

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63 274, Smith proclaimed: "Though the English do not lay exclusive claim to having discovered God, they do claim to have invented the trust with two natures in one." TB Smith (ed) *International Encyclopaedia of Comparative Law* (1976) 6 ch 2 para 262.

64 T Honoré "Trusts" in R Zimmerman & D Visser (eds) *Southern Cross: Civil Law and Common Law in South Africa* (1996) 849, endorsed in *Land and Agricultural Bank of South Africa v Parker* 2005 2 SA 77 (SCA) para 19.

65 From "*fief*" – "*n*. land held under feudal system or in fee; one's sphere of operation or control" W Brandford (ed) *The South African Pocket Oxford Dictionary* (1987) 276.

66 A shortened version of "*cestui a que use le feoffment fuit fait*" translated as "the person for whose use the *feoffment* was made". See, Anonymous "Definitions for Cestui que" (2019) *Definitions* <https://www.definitions.net/definition/Cestui%20que> (accessed 07-03-2019).

67 Hudson *Equity* 37.

treating it as his own.[68] The use therefore shared an important central characteristic with the modern trust, namely that control over the property was separated from the right to enjoy the benefits arising therefrom.

Initially the rights of the *cestui que use* were treated as a personal claim against the *feoffee t*o use,[69] with the property rights in question vesting in the *feoffee*.[70] The recurring theme in equity that a conscientious obligation takes priority over a strict legal right gave rise to the recognition that the *cestui que use's* right to compel compliance by the *feoffee* "constitutes an equitable estate in the property".[71] This recognition of proprietary rights in the hands of the *cestui que use*[72] necessitated the recognition of a duality of ownership, or "double *dominium*", with a distinction drawn between "legal" and "beneficial" ownership. Some English lawyers regarded this distinction in title as "the essential nature of the trust device".[73]

The use proved a popular mechanism for making over gifts to charities that were unable to own property. For example, as mentioned above,[74] in the thirteenth century Franciscan friars, who were bound by an oath of poverty and thus unable to own any land, established monasteries in England. Owing to their inability to own land, a wealthy benefactor would transfer property to the local borough community for "the use of" the friars.[75] Though technically the friars would not own the property, they were entitled to derive the benefit from such ownership.

Another advantage (and presumably the driving force behind the popularity of the use) was that a landlord could avoid the strict rules of inheritance and feudal dues through the mechanism offered by the use. If land was vested in a group of *feoffees*, who would never die as a group, the legal title would never have to pass to a successor and feudal incidents payable on inheritance could be avoided altogether.[76]

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68 Pearce & Barr *Equity* 14.

69 De Waal (2000) *SALJ* 553.

70 Pearce & Barr *Equity* 23.

71 *Re: Transphere (Pty) Ltd* 1986 5 NSWLR 309 311E-F.

72 Gray & Gray *Land Law* 76.

73 GL Gretton "Trusts without equity" (2000) 49 *Int Com LQ* 599 604. See also *Saunders v Vautier* (1841) 4 Beav 115; *Re Bowes* (1896) 1 Ch 507; *Baker v Archer-Shee* 1927 AC 844.

74 See the text to n 61 above.

75 Corbett (1993) *THRHR* 262.

76 Pearce & Barr *Trusts* 14.

The widespread popularity of the use, and its subsequent ill effects on the royal treasury, resulted in the passing of the Statute of Uses in 1535 intended to put an end to uses.[77] In cases where this statute applied, uses were "executed" by depriving the *feoffees* of their legal interest in the land and transferring such interest to the *cestui que use* in addition to the already held equitable interest. In this manner, the full ownership in the property was vested in the *cestui que use*.[78]

The trust form was saved from extinction through the ingenuity of lawyers who found ways to circumvent the Statute of Uses. That statute did not apply to a use where the *feoffee* had active duties to perform, such as the collection and distribution of profits or the management of an estate. The use form could also be saved through the creation of a "double use", termed a "use upon use". In terms of this construction, land would be conveyed to "X, to the use of Y, to the use of Z".[79] The first use, in respect of which land was conveyed to X was executed, vesting the entirety of the property rights in Y, but the obligation of Y to hold the property for Z was recognised by the chancery courts. This second use was termed a "trust" to distinguish it from the first and formed the basis of the modern terminology.[80]

The "use upon a use" developed into an important social tool that went further than merely the avoidance of taxes. For example, during the latter part of the sixteenth century the trust was employed to protect estates from spendthrift sons and to enable married women to enjoy property independently of their husbands.[81] In this manner, the social utility of the trust institution emerged.

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77 De Waal (2000) *SALJ* 553. There appears to be some debate about whether the Statute of Uses intended to put an end to the use. Albertus argues that the aim of the statute was merely to remove the division between legal and equitable ownership: Albertus (2014) *Acta Juridica* 270. Irrespective of the intention of the statute, it is uncontroversial to state that it severely restricted the use.

78 Garton *Moffat* (2018) 41.

79 See also Garton *Moffat* 42 for a discussion of the revival of the trust through the employ of a "use upon a use".

80 Pearce & Barr *Trusts* 15; Akkermans *Numerus Clausus* 340.

81 15.

2 3 Trusts in a civilian context

The distinguishing feature of the common-law trust, the splitting of ownership between legal and beneficial ownership,[82] is a product of equity. This distinction is unknown in jurisdictions based on civilian principles of property law.

However, this does not mean that the trust institution is incompatible with such systems. In two jurisdictions with civilian roots, in particular that of Scotland and South Africa, trusts have not only developed or been received, but have flourished.

2 3 1 Scotland

The exact origins of the trust in Scots law are uncertain.[83] What is clear is that the Scottish trust does not comply with the split-ownership concept central to the English trust.[84]

This is because the principle of duality of ownership is not present in a mixed jurisdiction such as that of Scotland where the law of property is founded upon civilian principles.[85] In Scotland and, as is discussed below, South Africa, the trustee holds absolute title over the trust property and the beneficiary only has a personal right against the trustee for the due fulfilment of his obligations.[86]

Gretton argues that the influence of the English trust in Scotland was minimal, and submits that it is entirely conceivable that the trust developed independently in Scotland.[87] In support of this submission, he points out that trust-like institutions existed in Scotland well before the seventeenth century. These arrangements were

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82 Described as the "essence of the trust" by the Privy Council in *Abdul Hameed Sitti Kadija v Da Saram* [1946] 208 (Ceylon) 217, where it quoted with approval RW Lee *Introduction to Roman-Dutch Law* 3 ed (1931) 372.

83 GL Gretton "Trusts" in K Reid and R Zimmerman (eds) *A History of Private Law in Scotland* (2000) 1 480.

84 Gretton (2000) *Int Com LQ* 619.

85 A mixed jurisdiction has been described as one resulting from the "fusion of the two great legal traditions of Europe, of the civil and the common law ...": see K Reid "National report for Scotland" in DJ Hayton, SCJJ Kortmann & HLE Verhagen (eds) *Principles of European Trust Law* (1999) 67. In both the cases of Scotland and South Africa, the law of property was born out of civilian principles, accounting for the rejection of the law/equity divide.

86 De Waal (2000) *SALJ* 554.

87 Gretton "Trusts" in *Private Law in Scotland* 485.

based on a concept akin to that of *depositum*, with the noted exception that not only possession, but also ownership, passed to the depositee.[88] Where the depositee was also instructed to deal with the property in a particular manner, aspects of *mandatum* entered the fray. In this regard, Gretton points out that seventeenth, eighteenth and nineteenth century commentators described the Scottish trust as based on principles of *depositum* and *mandatum*.[89] The fact that these institutional writers attempt to explain the Scottish trust on the basis of civilian principles as opposed to the, by then well known, common-law principles of duality in ownership is, for Gretton, indicative of the fact that the Scottish trust was not merely an English import.[90]

However, it is the inability of civil-law jurisdictions to conceptualise the trust on the basis of equity's principle of dual ownership that has led to severe criticism from common-law circles as to the authenticity of the civilian trust.[91] Of particular concern to common-law lawyers is the fact that, not possessing rights *in rem* in the trust property, beneficiaries are particularly susceptible to the possible insolvency of a trustee. The concern is based upon the assumption that owing to the fact that the trust property only vests in the trustee, the trustee's creditors will be able to lay claim upon such property flowing from obligations that do not bear any relation to the administration of the trust.[92]

Gretton has convincingly shown that this concern is no bar to accepting the civil-law trust as a "proper trust".[93] He points to the research of the French academic, Pierre Lepaulle, [94] who illustrated that the civilian tradition has always had

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88 489.

89 These include Stair, Erskine and Bankton. See Gretton "Trusts" in *Private Law in Scotland* 489.

90 Gretton "Trusts" in *Private Law in Scotland* 480 489:
"The significance of the characterization, in Stair and other writers, of trust as being a combination of mandate and deposit is that it lends support to the view that trust cannot be regarded simply as a seventeenth-century import from England. There is a continuity going back before 1600."

91 See DJ Hayton "Trusts" in DJ Hayton, SCJJ Kortman, AJM Nuytinck, AVM Struycken & NED Faber (eds) *Vertrouwd met de Trust: Trust and Trust-like Arrangements* (1996) 3; Gretton (2000) *Int Comp LQ* 600 and the commentaries discussed there.

92 Gretton (2000) *Int Comp LQ* 600.

93 610 n 61.

94 599.

appropriate concepts to protect the interests of beneficiaries without being required to adopt the principle of dual ownership that developed from equity. Referring to the Digest, Gretton highlights that the principle of patrimony (or *patrimonium*) was not only familiar in Roman law but also allowed for an individual to have more than one estate.

The concept of "patrimony" is well known in South African law, albeit under the style "estate", and denotes the totality of a person's assets and liabilities.[95] Gretton shows how Lepaulle, using the concept of patrimonies (or estates) and the appreciation that one person can have more than one estate, developed a theory which could support the existence of the trust in a civilian context.[96] According to this theory, each person has one, private, estate. However, where a person has been appointed as trustee a second, special, estate distinct and separate of the first arises – the trust estate.[97] In this manner, the assets in the trust estate are segregated from the trustee's personal estate.

For Gretton, the key to understanding the civilian trust lies in the above concept which he explains as follows:

> "Thus the assets of the special patrimony are segregated from the general patrimony, and to some extent the civilian tradition has likewise accepted segregation of liabilities also. Real subrogation is the key to the doctrine of patrimony, and patrimony is the key to trust. In other words, a trust is a special patrimony."[98]

In instances with multiple trustees, the trustees are joint owners of the special trust estate.[99] The specific type of joint ownership at hand, joint tenancy, accounts for what has been referred to as the "elastic" nature of ownership in trust property, as the removal of one trustee does not give rise to any formal or express transfer of ownership.[100]

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95 608.

96 Gretton (2000) *Int Comp LQ* 610; De Waal (2000) *SALJ* 560.

97 De Waal (2000) *SALJ* 560.

98 Gretton (2000) *Int Comp LQ* 610.

99 611.

100 MJ de Waal "The strange path of trust property at a trustee's death: theory and practice in the law of trusts" (2009) *TSAR* 84 91. For a discussion on this type of ownership, see part 5 4 1 in Chapter 5.

The distinguishing feature of the Scottish trust (compared to the English trust) is therefore that the whole of the ownership in the trust assets vests in the trustees, albeit that it is held in a different, separate, estate. The beneficiaries, therefore, only have personal rights against the trustees for the proper administration of the trust. The point that deserves emphasis is that holding the trust assets in a special estate protects the trust from the claims of the trustee's private creditors who are confined to satisfying their claims from the trustee's personal estate.

By necessary implication, the inverse position also holds true. A trustee's personal estate is also isolated and protected from claims by the trust's creditors who are confined to seek redress from the trust estate. In this manner, trusts provide the effect of limited liability also achieved through the incorporation of a separate juristic entity, with the notable distinction that a trust is not a juristic person.[101] It is the abuse of this feature that forms the basis of the discussions in Chapter 6.[102]

It is therefore clear that the principle of duality of patrimonies (or estates) is as central to the understanding of the civilian trust as the principle of split ownership is to the understanding of the common-law trust.

2 3 2 South Africa

The South African trust and its Scottish counterpart have been described as illegitimate siblings, but the origin of these two trusts is entirely dissimilar.[103] While it has been argued that the Scottish trust developed independently from its English counterpart,[104] there can be little doubt that the first trust to arrive on South African shores was an English trust.[105]

During the early nineteenth century, English settlers and officials brought the trust to South Africa "as part of their legal and intellectual baggage".[106] The trust was imported into South African civilian life by the use of the words "trust" and "trustee" in

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101 See, BS Smith "Statutory discretion or common law power? Some reflections on 'veil' piercing' and the consideration of (the value of) trust assets in dividing matrimonial property – Part One" (2016) 41 *JJS* 68 69.

102 See part 6 4 of Chapter 6.

103 E Cameron "Constructive trusts in South African law: the legacy refused" (1999) 3 *Edinburgh LR* 341.

104 Gretton "Trusts" in *Private Law in Scotland* 485.

105 Cameron (1999) *Edinburgh LR* 348. Cameron et al *Honoré* 26.

106 Honoré "Trusts" in *Southern Cross* 850, quoted by De Waal (2000) *SALJ* 555.

wills, deeds of gift, ante-nuptial contracts, and land transfers executed by these English settlers and officials. For nearly a century, the English trust was left to permeate through South African society, with its civil-law underpinnings, and only in 1915 were the courts for the first time called upon to decide whether the trust formed part of South African law, and if so, upon what basis.[107]

In *Estate Kemp v McDonald's Trustee* ("*Kemp*")[108] the then Appellate Division of the Supreme Court was confronted by a will drafted by an English lawyer and expressed in English phraseology. In the will, the testator bequeathed the residue of his estate to trustees of various trusts, established for this purpose.[109] A beneficiary to one such trust had died as an unrehabilitated insolvent and the question was whether her trustee in insolvency could lay claim upon her interest in the trust estate.[110]

The matter turned upon the nature of the beneficiary's right in the trust property. Significantly, Innes CJ held that the English law of trusts did not form part of South African law and that the dichotomy of split ownership was accordingly similarly foreign to South African law. This, however, did not mean that "testamentary dispositions couched in the form of trusts cannot be given full effect to in terms of our own [South African] law".[111]

The court held that the trust could be accommodated through the civil-law *fideicommissum*, and in particular the *fideicommissum purum*.[112] The significance of holding that the arrangement created in the will was that of a *fideicommissum* was that the beneficiaries did not have any rights *in rem* in relation to the trust property, but their rights were confined to personal rights against the trustee.

The view that a South African trust was a form of *fideicommissum* prevailed until 1984, when the Appellate Division reconsidered the nature of the South African trust in *Braun*.[113]

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107 Corbett (1993) *THRHR* 262.

108 1915 AD 491 498-506.

109 Cameron et al *Honoré* 15.

110 *Estate Kemp v McDonald's Trustee* 1915 AD 491 493.

111 499.

112 502.

113 1984 2 SA 850 (A).

That matter concerned a testamentary trust in terms of which the trustees were afforded discretionary powers of appointment to select the income and capital beneficiaries from a designated group.[114] The appellant, the testatrix's daughter, challenged the validity of the trust on the ground that the conferment of discretionary powers of appointment on the trustees was invalid and unenforceable in law. Consequently, the appellant contended that the portion of the testatrix's estate earmarked for the trust, was to devolve in terms of the rules of intestacy.[115]

It was argued on behalf of the appellant that South African law did not permit the conferment of such discretionary powers on trustees who have no interest in the trust property on account of Roman law requiring testators to execute their wills personally.[116] This matter therefore provided an opportunity to re-examine the nature of trusts in South African law.

The court again acknowledged the existence in South Africa of the trust institution, but held that it was both historically and jurisprudentially wrong to identify the trust with the *fideicommissum*.[117] Instead, the trust was described as "a legal institution *sui generis*".[118] Crucially, the court re-asserted that the dichotomy of dual ownership remained foreign to South African law and that beneficiaries only have personal rights against the trustee for the due fulfilment of their trust obligations.[119] The court expressed itself as follows:

> "the English law of trusts with its dichotomy of legal and equitable ownership (or 'dual ownership' according to the American law of trusts) was not received into our law. The English conception of an equitable ownership distinct from, but co-existing with, the legal ownership is foreign to our law. *Our Courts have evolved and are still in the process of*

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114 856E.

115 855C.

116 856G.

117 866B and 859B-C where the court expressed itself as follows:
"Admittedly, many of the functions which the *fideicommissum*, either by itself or in conjunction with other devices of the Roman law, performed, could have been performed by the trust had the latter been known to the Romans, but the fact remains that historically and jurisprudentially the *fideicommissum* and the trust are separate and distinct legal institutions, each of them having its own set of legal rules."

118 859.

119 859H.

evolving our own law of trusts by adapting the trust idea to the principles of our own law."[120]

The court ultimately held that the conferment of discretionary powers to select beneficiaries was permissible, and the appeal accordingly failed.[121]

The *Kemp*[122] and *Braun*[123] cases dealt only with testamentary trusts and it is clear that as far as these trusts are concerned, the South African trust is a *sui generis* institution that is evolving on the basis of civilian legal principles.

In relation to *inter vivos* trusts, South African courts have held in a series of judgments that such trusts are based on the civilian basis of the *stipulatio alteri* (a contract for the benefit of a third party).[124] In this manner, the principle that the rights of trust beneficiaries of an *inter vivos* trust are also merely personal in nature was confirmed.

Despite the differing histories of the South African and Scottish trusts, both jurisdictions refused to adopt the dichotomy of split ownership central to the English trust and instead opted to conceptualise the trust institution on the basis of the civilian underpinnings of their respective laws of property. The South African trust has therefore also adopted the principle of dual patrimonies vital to the Scottish trust, which serves to protect trust beneficiaries from the trustee's personal creditors.[125]

However, a comparison between Scots and South African law reveals one noticeable difference: Scots law requires, as a fundamental principle, that the trustee be the owner of the trust estate – there can be no other possibility.[126] South African law also recognises the "*bewind* trust" where the trust estate is made over to the

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120 859F-G (emphasis added).

121 866F-867F. The court, however, held that one of the provisions of the will, empowering the trustees to appoint capital beneficiaries, was invalid. Nevertheless, this invalidity did not stem from the power to appoint or select capital beneficiaries, but to establish further trusts in the event of a deceased beneficiary being survived by lawful issue. This was judged to amount to an impermissible delegation of will-making power: 867B-F.

122 1915 AD 491.

123 1984 2 SA 850 (A).

124 *Commissioner for Inland Revenue v Estate Crewe* 1943 AD 656; *Commissioner for Inland Revenue v Smollen's Estate* 1955 3 SA 266 (A) and *Crookes NO v Watson* 1956 1 SA 277 (A).

125 De Waal (2000) *SALJ* 561.

126 561.

beneficiaries with the *caveat* that control is placed in the hands of another, the trustee, who is required to administer the estate for the benefit of the beneficiaries.[127]

The recognition of the *bewind* trust was not uncontroversial. The *bewind* trust was derived from Dutch law relating to administration and was introduced by Afrikaner settlers and practitioners.[128] Honoré specifically recognised the *bewind* as a trust in the first edition of his book on trusts,[129] which attracted an "angrily propounded" rejection by CP Joubert, later Judge of Appeal in the Appellate Division and the author of the judgment in *Braun*.[130] Joubert referred to Honoré's views regarding ownership of trust property as "verbysterend" (perplexing) and "kettery" (heresy).[131]

Ultimately Honoré's views prevailed and this form of trust, which has received legislative recognition in the Trust Property Control Act 57 of 1988 ("TPCA"), underscores an important principle – that "control by the trustee/administrator rather than ownership is the essential feature of a trust".[132]

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127 Cameron et al *Honoré* 10.

128 T Honoré "On fitting trusts into civil law jurisdictions" in *Oxford Legal Studies Research Paper No. 27/2008* <https://papers.ssrn.com/sol3/papers.cfm?abstract_id=1270179> (accessed 04-08-2019).

129 AM Honoré *The South African Law of Trusts* (1966).

130 E Cameron "Preface" to Cameron et al *Honoré* vii. CP Joubert "'n Kritiese opvatting van Honoré se beskouings oor die trustreg" (1968) 31 *THRHR* 124 and CP Joubert "Honoré se opvatting oor ons trustsreg" (1968) 31 *THRHR* 262.

131 Joubert (1968) *THRHR* 131; MJ de Waal "Honoré's South African law of trusts" in D Visser & M Loubser (eds) *Thinking about Law: Essays for Tony Honoré* (2011) 38 42.

132 T Honoré & E Cameron *Honoré's South African Law of Trusts* 4 ed (1992) 4. The specific quotation above has been omitted from the fifth and sixth editions of this work, by its subsequent authors. However, the principle that it is the control over the assets that is the essential feature of the trust is explicitly endorsed. See Cameron et al *Honoré* (2002) 7 and Cameron et al *Honoré* (2018) 8. Erasmus, in his review of the third edition of Honoré's book expressed Honoré's influence as follows:
"From the outset, in the first edition, he stressed that the trustee or administrator in South African law need not be the owner, clothed with a bare legal title, of the trust assets. This viewpoint has at times elicited strong criticism but, in the end, the historical, jurisprudential and comparative analysis which underlies this conclusion is perhaps Honoré's greatest achievement and most important contribution." HJ Erasmus (1985) 102 *SALJ* 740 741.

2 4 The core elements of a trust

The existence, and flourishing, of South African and Scottish trusts disprove the contention that split ownership is a pre-requisite for the establishment of a trust. The principle of dual patrimony (or estates) has proven equally adept at protecting trust beneficiaries from the claims of creditors of the trustee's personal estate.

Against this background, De Waal attempted to identify the core elements of the trust and arrived, after a comparative analysis of the English, Scottish and South African trusts, at four core elements that must be present in order for an arrangement to qualify as a trust. These are: (i) the fiduciary position of the trustee; (ii) separation of estates; (iii) real subrogation; and (iv) trusteeship as an office.

These core elements underscore the separation of control by the trustees from the benefit that accrues to the beneficiaries, which is a feature of the development of the trust discussed above. They are discussed below.

2 4 1 The fiduciary position of the trustee

De Waal points out that the terms "trust" and "trustee" imply an obvious and fundamental truth: that the position of trustee is one of trust.[133] The fiduciary nature of the trustee obligation is discussed in further detail in Chapter 4, but for present purposes, it serves to underscore that a core element of the trust is that a trustee stands in a fiduciary position of trust to the beneficiaries.[134]

In England and Scotland, the law requires of a trustee in the administration of the trust to exercise "the same degree of diligence that a man of ordinary prudence would exercise in the management of his own affairs".[135] In South Africa, the trustee's duty appears to have initially been set somewhat higher. In *Sackville-West v Nourse*[136] the then Appellate Division required that a trustee must use greater care in the handling of trust property that he might in dealing with his own. The TPCA now requires that a trustee "shall in the performance of his duties and the exercise of his

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133 De Waal (2000) *SALJ* 557, referencing N Jones "Trusts in England after the Statute of Uses: A view from the 16th century" in R Helmholz & R Zimmerman (eds) *Itinera Fiduciae* (1998) 173 193.

134 Cameron et al *Honoré* 13.

135 De Waal (2000) *SALJ* 559, referencing the House of Lords in *Rae v Meek* (1889) 16 R (HL) 558 569.

136 1925 AD 516 553.

powers act with the care, diligence and skill which can reasonably be expected of a person who manages the affairs of another".[137]

Du Toit et al describe the contemporary South African trustee's duty as essentially entailing "that a trustee must undertake trust administration in good faith with the requisite care, diligence and skill to serve the best interests of the trust beneficiaries".[138]

2 4 2 Separate estates

As discussed above, the distinction drawn between legal and equitable ownership in equity ensures that beneficiaries are protected from the insolvency of the trustee. However, notwithstanding the concept of divided ownership, it is arguable that it is the consequence of the separation of *estates* that is decisive.

De Waal shows how the protection against creditors afforded to beneficiaries in English law is explained in terms of the "enduring equitable obligation concerning property"[139] which the trustee owes the beneficiary. In particular, De Waal points to the use of the term "patrimony" in the following explanation offered by Hayton:

> "The equitable proprietary rights of the beneficiaries in the trust property prevent such property from becoming part of the trustee's patrimony, so the beneficiaries' rights are not affected by the insolvency, divorce or death of the trustee".[140]

It therefore appears that it is this necessary consequence, rather than the division of ownership itself, that is the source of the protection of trust beneficiaries in English law, since the trust assets do not form part of the trustee's private estate.

Likewise, the separation between a trustee's private estate and the special trust estate in the civil law ensures protection from the insolvency, divorce, or death of the trustee. The separation of private and trust estates in South Africa has also received legislative approval in the TPCA which, in section 12, provides that:

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137 Section 9(1) of the TPCA.

138 Du Toit et al *Fundamentals* 4.

139 De Waal (2000) *SALJ* 560, referencing Hayton et al *Principles of European Trust Law* 67.

140 De Waal (2000) *SALJ* 560, quoting Hayton "Trusts" in *Vertrouwd met de Trust* 4.

> "Trust property shall not form part of the personal estate of the trustee except in so far as he as trust beneficiary is entitled to the trust property".

2 4 3 Real subrogation

A further core element of the trust is the operation of "real subrogation". Real subrogation refers to the concept that the turn-over in trust assets remains within the trust estate. De Waal explains this as follows:

> "once one accepts that there are two separate estates, there must be a mechanism to deal with the obvious eventuality of a replacement of (or turn-over in) assets in the trust estate. This mechanism is found in the concept of real subrogation. Real subrogation simply means that the proceeds of a trust asset (if the asset has been sold) or the substitute asset (if the proceeds have been used to buy something else) will also be subject to the trust. One could also say that the proceeds or the substitute, as the case may be, will form part of the trust estate. Real subrogation, therefore, 'ensures the continuity of the trust estate'".[141]

From a South African perspective, the above principle is uncomplicated: the turn-over, or growth, in assets held in the trust estate accrues to that estate. This is because in South Africa, real subrogation is limited to lawful transactions.[142] It is when the principle of real subrogation is extended to unlawful transactions that matters become altogether more complex.

In English law, real subrogation transcends lawful exchanges of trust property through a network of rules relating to "following", "tracing" and "constructive trusts". [143] The principles underlying tracing and constructive trusts make for interesting reading and the application thereof in a civilian context has been questioned.[144] These principles however do not form part of the South African trust law[145] and, consequently, fall outside the scope of this research.

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141 De Waal (2000) *SALJ* 564; T Honoré "Obstacles to the reception of trust law? The examples of South Africa and Scotland" in AM Rabello (ed) *Aequitas and Equity: Equity in Civil Law and Mixed Jurisdictions* (1997) 739 805.

142 De Waal (2000) *SALJ* 564.

143 Hudson *Equity* 487-582; Garton *Moffat* 22-26; Pettit *Equity* 190-200; Pearce & Barr *Trusts* 946-993.

144 See GL Gretton "Constructive trusts: I" (1997) 1 *Edinburgh LR* 281 285.

145 Cameron (1999) *Edinburgh LR* 341.

2 4 4 Trusteeship as an office

The concept of trusteeship as an office is credited to Honoré, the "principal architect of modern South African trust law",[146] and is in my view his single most significant contribution to the South African law of trusts.[147]

As appears more fully in the chapters that follow, it is the appreciation that the trustee occupies a *quasi*-public "office" that distinguishes it from a purely private law institution and which forms the basis of the propositions advanced in this research.[148]

The description of trusteeship as an office denotes that the trustee administers the trust in an *official*, rather than *private*, capacity.[149] This means that, although the trust is not a juristic person, and the trust estate can only be bound by the conduct of the trustees, all acts of trustees occur through the office of trusteeship.

The metaphor of a cloak is appropriate. The office of trusteeship is the cloak that is filled by the trustee's person and which empowers the trustee to act. It is through this proverbial garment, attached to the trust deed, that the trustee's powers and obligations flow – only persons occupying the office of trusteeship are empowered to act as such and compelled to exercise the obligations attaching to that office.

The most significant manifestation of the office of trusteeship lies in the oversight role that the courts and the Master play in contrast to other private law arrangements. In *Genesis Medical Aid Scheme v Registrar, Medical Aid Schemes*[150] the Constitutional Court recognised the significance of this as follows:

> "Once established, a trust creates a legal relation of fiduciary obligation on the part of the trustee towards the beneficiary. That relation is distinct from a purely contractual or

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146 De Waal (2000) *SALJ* 565. See also Du Toit et al *Fundamentals* 25 where Honoré is described as "the leading light in the scholarly development of [South African] trust law".

147 Honoré died on 26 February 2019, but the impact of his contribution to South African trust law is set to remain indefinitely. In the latest *Festschrift* written in his honour (in total there were three) De Waal, commenting on the (then) imminent publication of the sixth edition of *Honoré's South African Law of Trusts* wrote: "Since its fourth edition the title of Honoré's book has been *Honoré's South African Law of Trusts.* This is more than the title of a book: it is also a statement of fact. The South African law of trusts is and indeed will remain Honoré's". De Waal "Honoré's South African law of trusts" in *Thinking about Law* 49.

148 Cameron et al *Honoré* 14.

149 Du Toit et al *Fundamentals* 3.

150 2017 6 SA 1 (CC).

> commercial relationship. This is because a trustee occupies a fiduciary office that is subject to supervision and regulation by the courts. Even in a consensual trust, the trustee is not simply a contracting party, but assumes an office subject to court supervision and public control, as no contractant does."[151]

The supervision over the office of trusteeship is rooted in both common law and statute. At common law, a court has the power to remove a trustee from office if such removal is in the interests of the beneficiaries,[152] or appoint replacement trustees in circumstances where the office has become vacant (through, for example, death or resignation).[153]

The TPCA also contains several provisions that underscore the public nature of the office of trusteeship, for example: the requirement that trusts be registered with the Master;[154] the provision that a person shall act as trustee only if authorised thereto by the Master;[155] the provisions regarding the furnishing of security;[156] the power of the courts to vary trust provisions and to terminate trusts;[157] the power of the Master to call upon trustees to account,[158] and the power of the Master to remove trustees from office.[159]

Honoré summarises the position as follows:

> "The court in the last resort will not merely see that remedies are granted for breach of trust – as it would for the breach of ordinary contracts – but that the necessary arrangements are made for trusts to be carried out according to their terms, something that it will not do for ordinary contracts."[160]

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151 Para 30.

152 *Letterstedt v Broers* (1884) 9 AC 371; *Sackville West v Nourse* 1925 AD 516; *Volkwyn NO v Clarke and Damant* 1947 (WLD) 456; *Tijmstra NO v Blunt-MacKenzie NO* 2002 1 SA 459 (T).

153 De Waal (2000) *SALJ* 566.

154 Section 4(1). Interestingly, the TPCA, including this provision, does not apply to oral trusts. *Deedat v The Master* 1995 2 SA 377 (A).

155 Section 6(1).

156 Section 6(2) and 6(3).

157 Section 13.

158 Section 16.

159 Section 20.

160 De Waal (2000) *SALJ* 566, quoting T Honoré "Obstacles to the reception of trust law? The examples of South Africa and Scotland" in AM Rabello (ed) *Aequitas and Equity* (1997) 805.

These powers of oversight distinguish the trust from any other private law institution. To place matters in context, it is unthinkable that a court could (or would) remove a party to a private agreement on account of breach; replace them with another party; or unilaterally vary the terms of an agreement to give effect to the purpose thereof.

2 5 *Land and Agricultural Bank of South Africa v Parker*

Perhaps the most significant judicial commentary on the South African trust and the principles that underpin it to appear in the past three decades is the judgment by the SCA, written by Cameron JA (as he then was), in *Land Bank v Parker*.[161] A cursory review reveals that it has been cited with approval (as of January 2019) in no less than 27 subsequent reported, and no doubt countless more unreported, judgments.[162]

The judgment is significant because it confirms the functional separation between the control over and the enjoyment of a benefit as the "essential notion of trust law" from which its further development is to proceed.[163] In addition, it gives valuable guidance on the significance of the trust deed, the joint-action rule,[164] and the dangers concomitant upon the abuse of the trust in family and business dealings. For those reasons, a brief review of *Land Bank v Parker* is a pre-requisite for any meaningful discussion on the further development, and theoretical principles, underpinning the trust.

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161 2005 2 SA 77 (SCA).

162 This number refers to the South African Law Reports. *Land Bank v Parker* has also, however, been referenced numerous times in the All South African Law Reports, and by the Southern African Legal Information Institute's (SAFLII) online repository at www.saflii.org. When these references are included, the number of reported judgments relying on *Land Bank v Parker* (taking into account potential overlap) exceeds 27 by far.

163 Para 22. See also Cameron et al *Honoré* 21.

164 The joint-action rule dictates that, in the absence of a contrary provision in the trust deed, the trustees must act jointly if the trust estate is to be bound. This rule is described in detail in Chapter 5. See part 5 4.

The matter concerned the enforceability of a suretyship agreement concluded between the trustees of the Jacky Parker Trust ("the trust") and the Land and Agricultural Bank of South Africa ("the bank").[165]

The trust was a family trust established in 1992 by a commercial farmer, DW Parker ("Parker Snr"), for the benefit of himself and his wife, for whom the trust was named, and their descendants. The first trustees were the Parkers and their family attorney, Senekal, who resigned in 1996.[166]

The trust deed contained a provision to the effect that there would at all times be no fewer than three trustees in office and that the remaining trustees would, in such event, be empowered to appoint a replacement trustee. Notwithstanding these provisions, the Parkers failed for almost two years after Senekal's resignation to take any action and only informed the Master thereof in June 1998.[167]

Between April and October 1998, the Parkers, acting alone, purported to bind the trust as surety and co-principal debtor in a series of agreements in terms of which companies associated with their farming enterprise obtained significant loans from the bank. By the time the last of these agreements were concluded, the Parkers had appointed their son, DG Parker ("Parker Jnr") as a replacement trustee on direction of the Master. The evidence revealed that Parker Jnr played no part in the conclusion of this last agreement, which involved a loan of R30 million from the bank.[168]

Eventually matters went wrong and the bank commenced sequestration proceedings against the Parkers and the trust. It obtained provisional sequestration orders against the trust and Parker Snr[169] during September 2000, which were

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165 Para 4.

166 Para 2.

167 Para 3.

168 Para 4.

169 The application against Mrs Parker was unsuccessful on the basis that the bank was unable to prove an advantage to creditors. In terms of ss 10(c) and 12(1)(c) of the Insolvency Act 24 of 1936 ("the Insolvency Act"), a court may not grant a sequestration order unless "there is reason to believe that it will be to the advantage of creditors of the debtor if his estate is sequestrated".

confirmed on 27 October 2000.[170] Since a clause of the trust deed provided that upon insolvency, a trustee's trusteeship is automatically terminated,[171] Parker Snr ceased to be a trustee upon his sequestration. However, he continued to act as trustee and sought leave to appeal in both his own capacity and on behalf of the trust, which was refused by the court of first instance. A petition to the SCA followed, and only the trust was granted leave to appeal to the Full Bench.[172]

The primary contention on behalf of the trust in the Full Court was that the Parkers, on their own, did not have the power to bind the trust estate in concluding the suretyship agreements with the bank.[173] This defence was upheld on the basis that, in the absence of three trustees as required by the trust deed, the trustees did not have the power to act.[174] A petition by the bank followed and leave to appeal to the SCA was granted.

The factual matrix required a distinction to be drawn between the scenario prior to Parker Jnr's appointment and that after his appointment. In respect of the position

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170 The Insolvency Act distinguishes between "provisional" and "final" sequestration: A Boraine, JA Kunst & DA Burdette *Meskin on Insolvency Law* (SI 51 2018) 2-18 explain the rationale for the distinction as follows:
"The reason for this is that not only the interests of the applicant and the debtor, but also the interests of all the debtor's creditors, are affected when a sequestration order is granted: while, therefore, the creditor able to establish a prima facie case for sequestration, is to have the benefit of preservation of the debtor's property, an opportunity is to be afforded to the debtor and all his other creditors to be heard in relation to the issue of whether a final order of sequestration should be granted."

171 Para 39.

172 Para 5.

173 Para 6.

174 The appeal process was at this time regulated by the provisions of the Supreme Court Act 59 of 1959. In accordance therewith, an unsuccessful litigant was afforded an opportunity to apply for leave to appeal in the court of first instance, whereupon leave could either be refused or granted to the Full Bench or the SCA. The "Full Bench" refers to a bench of three judges in the court of first instance, appointed by the Judge President of the court concerned. If leave was refused, the unsuccessful litigant was permitted to deliver a "petition" to the SCA seeking leave to appeal. That court was similarly empowered to either refuse the petition, grant leave to the Full Bench, or itself. The Superior Courts Act 10 of 2013 now regulates this position. This Act restructured the High Courts into divisions of a single High Court. The appeal process has however remained unchanged, save for a change in terminology. "Application" is now made to the SCA for leave to appeal to either that court or the "Full Court" of the relevant "Division" of the High Court.

prior to Parker Jnr's appointment, the bank relied on the general contention that all the trustees in office, acting jointly, could bind the trust. Regarding the position after Parker Jnr's appointment, the bank contended that as the trust deed authorised majority decision making, the Parkers, representing a majority of trustees, could bind the trust without the co-operation of their son.[175]

In rejecting the bank's contentions, the SCA elucidated the correct approach to questions of trustee capacity. The first principle is that a trust does not enjoy separate legal personality but constitutes a collection of assets and liabilities arranged in an estate. Therefore, in order for the estate to be bound, action by the trustees is required. However, as the power of the trustees flows from the provision of the trust deed, which is described as "the constitutive charter" of the trust, a trust cannot be bound outside its provisions.[176]

Therefore, where the trust deed required a minimum number of trustees in office, this constituted a so-called "capacity-defining" condition without which the trust could not act.[177] The necessary implication was that, while the Parkers were the sole trustees, the body of trustees suffered from an incapacity and the agreements purportedly concluded by them during that time were therefore void.

After the appointment of Parker Jnr, this incapacity was cured. However, as is discussed in more detail in Chapter 5,[178] it is a fundamental rule of trust law that trustees are to act jointly. As the Parkers did not in any way involve Parker Jnr in the conclusion of the relevant agreements after his appointment, those agreements were void for failure of the trustees to act jointly.[179]

The bank's submission that the Parkers constituted a majority of trustees and could hence bind the trust without the son's concurrence, was therefore rejected. Central to the rejection of this argument was the principle that the majority of trustees formed only a complement of the whole. Therefore, while the majority could compel the trustees to act in a particular manner by virtue of the provision in the trust deed, this did not empower them to act alone.[180]

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175 Para 7.

176 Para 10.

177 Para 11.

178 See the text to part 5 4 of Chapter 5.

179 Para 18.

180 Para 17.

Based on these observations it followed that the bank's principal arguments had to fail and that the reasoning of the Full Bench was to prevail. There was however a single alternative argument – that the conditions in the peculiar case merited "going behind" the trust.[181] It is perhaps in the discussion of this alternative that the SCA gave its most significant direction to the future development of trust law in South Africa. The SCA confirmed that:

> "The core idea of the trust is the separation of ownership (or control) from enjoyment. Though a trustee can also be a beneficiary, the central notion is that the person entrusted with control exercises it on behalf of and in the interest of another."[182]

and that:

> "The essential notion of trust law, from which the further development of the trust form must proceed, is that enjoyment and control should be functionally separate. The duties imposed on trustees, and the standard of care exacted of them, derive from this principle."[183]

Ultimately however, this argument was not followed through as it was not the case presented by the bank. The bank relied and also failed on the argument that the Parkers, acting alone, could bind the trust estate.

However, while the trustees' argument was accepted, there was an ironic, but just, twist. Due to the principle that the trustees could only act in circumstances where there were three trustees, it transpired that the application for leave to appeal to the Full Bench was defective. This was so because Parker Snr had automatically ceased to be a trustee upon his sequestration. The failure of Mrs Parker and Parker Jnr immediately to appoint a replacement trustee therefore resulted therein that the trustees were not empowered to prosecute the appeal to the Full Bench. The result was that the trust was therefore never before the Full Bench and that its decision was to be set aside. The (strictly speaking incorrect) decision of the court of first instance was therefore to be reinstated.[184]

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181 Disregarding the trust estate is discussed in detail in Chapter 6. See in particular the text to part 6 4.

182 Para 19.

183 Para 22.

184 Paras 36-45.

It followed that, in the end, the trust was held liable for the debts owing to the bank through the consistent application of its own argument.[185]

2 6 Conclusion

The historical development of the trust reveals a universal human desire for the establishment of a legal institution through which others can safeguard the beneficial interests of those that are not in a position to do so themselves. This is achieved through the functional separation between control and benefit.

As a result of diverse historical developments, this functional separation is achieved differently in jurisdictions with a common-law based property regime as opposed to those with a civil-law property regime.

The common law recognises a split ownership of trust assets, with legal ownership vesting in the trustees and the beneficial ownership vesting in the beneficiaries. This provides the basis upon which control over the trust assets is vested in the trustees, but also ensures that all benefit that arises accrues to the beneficiaries.

Civil-law jurisdictions do not recognise the split ownership inherent in the common-law trust and the whole of the ownership of the trust estate vests in the trustee.[186] However, the same separation between control and benefit (and ultimate protection of beneficiaries) is achieved as in the common law by recognising that the trust estate is separate from that of the trustee's personal estate.

The effect of the separation of the trust estate from that of the trustee's personal estate is that the latter estate is protected from the trustee's personal creditors, thereby also providing a mechanism that achieves the insulating effects of separate juristic personality in corporate law.

There are four core elements of a trust, namely: (i) that the trustee is to stand in a fiduciary position; (ii) that there must be a separation of estates; (iii) the operation of real subrogation; and (iv) trusteeship as an office.

Of these elements, trusteeship as an office provides the theoretical underpinning for the majority of the questions examined in this dissertation.

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185 Cameron et al *Honoré* 380-382.

186 Except for the *bewind* trust discussed above.

CHAPTER 3: A THEORETICAL BASIS FOR THE PRINCIPLE OF TRUSTEE INDEPENDENCE – THE INDEPENDENCE DUALITY

3 1 Introduction

It is widely accepted that a trustee has a duty to exercise independent judgement in the fulfilment of his duties.[1] However, the exact theoretical basis for this duty is uncertain and is a subject of debate.[2]

This chapter identifies two principal propositions advanced for the theoretical basis of a trustee's duty of independence namely the "establishment proposition" and the "fiduciary proposition".[3] It proceeds to show how these propositions are not mutually exclusive but, in fact, complementary in that each provides an accurate explanation for one peg of what is described as "the independence duality" model.

The independence duality model emphasises that the evaluation of trustee independence is a two-step process. First, the trustee is to be afforded the capacity to act independently, and secondly, the relevant trustee must exercise this capacity. It is only when both these requirements are met that it can be said that a trustee acts independently. This model, and its relationship with the establishment and fiduciary propositions, provide the vital backdrop against which questions regarding trustee independence may be examined, including, significantly, the relationship between trustee independence and so-called "sham trusts"[4] and "going behind the trust", or as is discussed, "disregarding the trust estate".[5]

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1 *PPWAWU National Provident Fund v Chemical, Energy, Paper, Printing, Wood and Allied Workers Union* 2008 2 SA 351 (W); *Afrisure CC v Watson NO* 2009 2 SA 127 (SCA); MJ de Waal "The liability of co-trustees for breach of trust" (1999) 10 *Stell LR* 32; F du Toit "A trustee's duty of independence" (2009) 72 *THRHR* 637.

2 L Theron "Die besigheidstrust" (1991) 2 *TSAR* 268; M Honiball & L Olivier *The Taxation of Trusts in South Africa* (2009) 253; PA Olivier *Trustreg en Praktyk* (1989) 37; Du Toit (2009) *THRHR* 637; PA Olivier, S Strydom & GPJ van den Berg *Trust Law and Practice* (SI 6 2018) 2-15.

3 The terms "establishment proposition" and "fiduciary proposition" are entirely my own. However, the positions adopted by the principal advocates for each proposition discussed in this chapter are in keeping with the descriptions as formulated herein and attributed to them.

4 The term "sham trusts" has been used to describe the position where the trust was used to merely mislead, see M Conaglen "Sham trusts" (2008) 67 *CLJ* 176. However, as is argued in Chapter 6, there is no such thing as a "sham trust". It is proposed that the

Before the independence duality model, its constituent parts, and the way they relate to the establishment and fiduciary propositions can be fully explored, the aforementioned propositions, as presented by their respective principal advocates, must first be investigated.

Accordingly, the establishment and fiduciary propositions as they presently stand will be explored, after which the duality in trustee independence will be highlighted.

Based on this duality, the manner in which each of the establishment and fiduciary propositions relate to trustee independence is examined. In this respect, it is argued that the establishment and fiduciary propositions are ineffective to the extent that they each purport to offer a comprehensive justification for the broad concept of trustee independence. However, in acknowledging the independence duality, these two propositions each underpin an important, but conceptually distinct, aspect thereof.

3 2 The principal propositions

A review of academic commentary relating to trustee independence reveals two, at first glance mutually exclusive, propositions. These propositions, the "establishment" and "fiduciary" propositions, approach the question of trustee independence from two different perspectives and both appear to find support in existing case law and academic commentary.

In brief, the establishment proposition holds that trustee independence is a fundamental requirement for the validity of a trust.[6] Therefore, an arrangement where a trustee's capacity to bring an independent mind to bear upon the administration of the trust is jeopardised, will not qualify as a trust.[7] The term "establishment proposition" is derived from this central tenet of this proposition.

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sham doctrine, and its South African counterpart the "simulation doctrine", are ill-suited to the law of trusts and the establishment proposition is preferred to examine those cases where "trusts" are purportedly established only to deceive. See part 6 3 in Chapter 6 and the authorities cited at n 24.

5 See part 6 2 of Chapter 6.

6 JA Crane & AR Bromberg *Crane and Bromberg on Partnership* (1968) 174-176; Theron (1991) *TSAR* 268; M Honiball & L Olivier *The Taxation of Trusts in South Africa* (2009) 253.

7 See Theron (1991) *TSAR* 285 for examples where it had been suggested that a lack of trustee independence reduces the arrangement to that akin to partnership.

The fiduciary proposition also recognises the importance of trustee independence but rejects it as a pre-requisite to establish a trust. Instead, proponents of this proposition suggest that trustee independence is a facet of a trustee's fiduciary duty.[8] Consequently, a failure by a trustee to bring an independent mind to bear upon the administration of the trust does not invalidate the trust but constitutes a fiduciary breach. It is accordingly appropriate to describe this proposition as "the fiduciary proposition".

The question regarding which one of these two propositions accurately provides the theoretical basis for the imperative of trustee independence is significant as it is determinative of the consequences that follow where trustee independence has been compromised.

For example, if the establishment proposition is preferred and trustee independence is regarded as a pre-requisite for the validity of a trust, it follows that a lack of trustee independence would compromise the validity of the trust as a whole. Conversely, if it were to be accepted that trustee independence is not a pre-requisite for validity, but a constituent part of a trustee's fiduciary duty, a trustee's failure to act independently would not invalidate the trust, but may instead found a claim against the trustee for breach.

It is consequently clear that the theoretical basis for trustee independence plays an important role in determining the consequences of a lack of trustee independence.

At face value, these two propositions appear mutually incompatible. Either trustee independence is a requirement to establish a trust, or it is not. However, notwithstanding this apparent incompatibility, it is suggested that these propositions are not mutually exclusive, but complementary, and that each proposition provides a sound theoretical basis for two related, but significantly distinct, aspects of trust administration. Therefore, it is argued that there exists a duality in the concept of trustee independence that is overlooked by the principal advocates of each proposition. As mentioned above, this duality entails the principle of "independent trustee control" on the one hand, and the independent "exercise of trustee control" on the other. The acknowledgement of this duality permits the development of a theoretical model for understanding the underpinnings of trustee independence.

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8 Olivier *Trustreg* 37; Du Toit (2009) *THRHR* 637; Olivier et al *Trust Law* 2-15.

Hence in this dissertation this model is referred to as the "independence duality" model.

In terms of this model, the establishment proposition explains the theoretical basis for requiring that trustees be afforded the *capacity* for independent control, whereas the fiduciary proposition provides the same for the requirement that trustees *exercise* their control in an independent manner. The independence duality model, it is argued, therefore provides a basis upon which the broad concept of trustee independence can be explained and serves as a point of departure in any examination of trustee independence.

3 3 The propositions explored

The two propositions that form the basis of the independence duality model appear mutually exclusive on account of each seeking to clarify one, distinct, aspect of the independence duality.

It is this difference in focus that accounts for the perceived conflict between these propositions and the manner in which each is employed. Once these propositions are examined within the context of the independence duality, it is clear that each provides a sound theoretical basis for one aspect relating to trustee independence.

3 3 1 The establishment proposition

As appears from Chapter 2,[9] the development of the trust was premised upon the separation of control over the trust assets from the benefit derived therefrom, and it is this principle that lies at the centre of the trust institution.[10]

It is now settled law that for a valid trust to be formed, the founder should divest himself from control over the trust property.[11] As also discussed in Chapter 2, Cameron JA in *Land Bank v Parker*[12] described the separation of control over and enjoyment of the trust assets as the "core idea" of the trust. He continued by labelling

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9 See part 2 2in Chapter 2.

10 *Ex parte Leandy NO* 1973 4 SA 363 (N) 368F; *Land and Agricultural Bank of South Africa v Parker* 2005 2 SA 77 (SCA); F Du Toit *South African Trust Law: Principles and Practice* 2 ed (2007) 62; Olivier et al *Trust Law* 2-14.

11 E Cameron, M de Waal & P Solomon *Honoré's South African Law of Trusts* 6 ed (2018) 21.

12 2005 2 SA 77 (SCA).

trustee independence a consequence of this separation and considered it "an indispensable requisite of office".[13] This reference to trustee independence has suggested to some that trustee independence must be viewed as an essential requirement for the validity of a trust.[14]

In the third edition of his work on trust law, Honoré also lists "a degree of independence on the part of the trustee" as an element that is necessary for the existence of a trust.[15] Subsequent editions of that work have resisted claiming that trustee independence is necessary for the existence of a trust, but in the latest edition, Cameron et al go as far as to state that a trustee must have "a certain degree of independence".[16]

The principal advocate for the establishment proposition, L Olivier,[17] argues more directly that trustee independence is a pre-requisite for the validity of a trust.[18] For her, trustee independence is an essential requirement of a trust and she argues that, where such independence is lacking, no trust comes into existence but that the arrangement is akin to that of agency.[19] Cameron et al echo this submission and suggest that "[a] person who in administering property is bound by the instructions of another, for example the founder or beneficiaries, is an agent rather than a trustee".[20]

In support of this submission, Olivier points to USA case law suggesting that, where beneficiaries have effective control over the trustees and by implication the administration of the trust estate, a valid trust is not established, but that the trustees may be regarded as partners.[21]

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13 Para 22.

14 Honiball & Olivier *Taxation of Trusts* 248.

15 T Honoré *The South African Law of Trusts* 3 ed (1985) 6.

16 Cameron et al *Honoré* 14.

17 Formerly Theron.

18 Theron (1991) *TSAR* 287.

19 285.

20 Cameron et al *Honoré* 14.

21 The cases cited by her are: *Priestly v Treasurer & Receiver General* 120 NE 100, 230 Mass 452 (1918); *Simon v Klipstein*, DC NJ 1920, 262 Fed 823; *Downey Co v Whistler* (1933) 1988 NE 243, 284 Mass 461 and *Brown v Bedell* (1934) 188 NE 641 263 NY 177; *Kadota Fig Association of Producers v Case-Swayne CO* (1946) 73 Cal App 2d 796 167 P2d 518; *Engineering Service Corporation v Longridge Investment Co* (1957) 153 Call App 2d 404 314 P2d 563; *Bariffi v Longridge Development Corporation Co* (1958) 156

The reference to a partnership as the alternative to a trust may be puzzling from a South African perspective, but this reference must be viewed in the context of the commercial arrangements prevalent in the USA during the early nineteenth century.

One such arrangement is the so-called "joint-stock company". The description "joint-stock company" is misleading. Depending on the jurisdiction, a joint-stock company is not a corporation or company at all, but a partnership. This is the case in the USA, but not in England.[22]

The joint-stock company has its roots in England and in the conventional partnership where each partner brings into the partnership capital or skill.[23] In circumstances where the capital funding requirement for a particular venture required a large number of partners, a structure developed whereby the partners delegated management authority of the partnership to a smaller number among them (that is, a management committee).[24] To make this structure more attractive, the interest therein was agreed to be freely transferable.[25] Accordingly, the joint-stock company has been defined as:

> "an association in which the capital is thrown into one mass employed for the general benefit, each member participating in the gain according to the proportion of stock or capital which belongs to him."[26]

Call App 2d 583 320 P2d 192. See also the discussion of the "control test" in the context of USA case law in part 4 3 in Chapter 4.

22 Joint-stock companies were introduced to the USA through English law and, prior to the introduction of the Joint Stock Companies Act of 1844, were also considered a partnership in the UK.

23 R Bubb "Choosing the partnership: English business organisation law during the industrial revolution" (2015) 38 *Seattle U L Rev* 377 341.

24 The structure of a joint-stock company is described in detail in: A Du Bois *The English Business Company After the Bubble Act, 1720-1800* (1938) ch 4. See also LCB Gower *Principles of Modern Company Law* 4 ed (1979) chs 2-4 and R Harris *Industrialising English Law: Entrepreneurship and Business Organization, 1720-1844* (2000) 110.

25 The legality of transferring interests in these partnerships was confirmed in the 1840s. See *Garrard v Hardey* (1843) 5 Man & G 471 134 ER 648 and *Harrison v Heathorn* (1843) 6 Man & G 81 134 ER 817.

26 W Wait *A Treatise Upon Some of the General Principles of the Law: Whether Legal, or of an Equitable Nature, Including Their Relations and Application to Actions and Defences in General, Whether in Courts of Common Law, Or Courts of Equity; and Equally Adapted to Courts Governed by Codes.* IV (1885) 159.

Significantly, and unlike a trust, the liability of the beneficial members of a joint-stock company was not limited and they remained liable in general, as partners, to third parties to the full extent of the indebtedness of the collective.[27] In order to facilitate matters, the property of the joint-stock company was vested in the name of one or more "trustees". These trustees were so-called "bare trustees" who were subject to the direction of the management committee. It has been argued that this structure was the immediate ancestor of the modern corporation,[28] but despite it being more complex in structure than a traditional partnership, the joint-stock company was nevertheless a partnership.[29]

The key feature of the joint-stock company was that it provided a mechanism to source investment for return. For most of the period associated with the Industrial Revolution in England, the incorporation of a juristic entity could only be achieved through a petition to Parliament or the Crown. Potential competitors of such petitioners often raised objections on the basis of "public interest" and frequently successfully lobbied for the proposed incorporation to be rejected.[30]

This difficulty concerning incorporation of companies resulted therein that joint-stock companies gained popularity to such an extent that they were regulated by statute.[31] These statutes had the effect of deeming joint-stock companies, formed

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27 160.

28 See RDM Flannigan "The control test of principal status applied to business trusts: Part I" (1986) 8 *Est & Tr Q* 37 41.

29 See *Playfair Development Corp Pty Ltd v Ryan* (1969-70) 90 WN (NSW) 504.

30 Bubb (2015) 38 *Seattle U L Rev* 377 342. See also A Schall "Corporate governance after the death of the King – the origins of the separation of powers in companies" (2011) 8 *ECFR* 476 481.

31 Joint Stock Companies Act of 1844 (promulgated by statute 7 & 8 of Victoria, Chapter 110) ("Joint Stock Companies Act"). The aversion against incorporation has its roots in the South Sea Bubble. In the period between 1690 and 1725 three chartered businesses which operated by virtue of Royal decree rose to ascendancy, namely: The East India Company; the Bank of England and the South Sea Company. In 1720, the South Sea Company collapsed resulting in the "South Sea Bubble". In the wake of the ensuing financial collapse and market scandals, the English Bubble Act of 1720 was passed, rendering it illegal to trade in shares of unincorporated joint-stock companies. See R Harris "The Bubble Act: its passage and its effects on business organizations" (1994) 54 *J Econ Hist* 610.

and registered in a prescribed manner, quasi-corporations.[32] However, in the USA, where there was no similar statutory regulation, joint-stock companies have retained their nature as a form of partnership.[33]

Consequently, where an arrangement between "trustees" is identified as a joint-stock company, as opposed to a trust, those trustees were personally liable for the debts of the undertaking in question.

As is demonstrated in Chapter 4, a "control test" has been developed in the USA, the defining characteristic of which is that the trustee must have the capacity to exercise independent control over trust administration.[34] This test ascribes liability for corporate conduct to the true controllers of a juristic entity or collective and has its origins in distinguishing between so-called "true trusts" and joint-stock companies.[35] To illustrate, L Olivier refers to the following passage in Crane and Bromberg's work on partnerships:[36]

> "The distinction between the trust (in which there is no personal liability) and the partnership (in which there is) has been held to depend on whether the beneficiaries have power of control of management by the trustees. *The concern is whether management is vested in the trustees as principals or as agents of the beneficiaries*. Liability naturally follows if the beneficiaries are regarded as principals. What degree of control renders the beneficiaries principals is not altogether certain. Important factors are powers to instruct trustees, to remove them, to alter, amend or terminate the trust, to elect trustees periodically or fill vacancies. (Ironically, some of these are enjoyed by corporate shareholders without sacrificing their limited liability). Under this more liberal view, the terms of the trust instrument are important, although actual operation (as distinct from formal power) will be scrutinized in search for control."[37]

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32 Section 2 of the Joint Stock Companies Act. The same section also included under the term "joint-stock company" all life, fire and marine insurance companies, and every partnership consisting of more than twenty-five members. See, T Parsons & WV Kellen *Law of Contracts* (1883) 162 n (a).

33 For a brief description of the introduction and development of joint-stock companies in the USA, see MM Blair "Reforming corporate governance: what history can teach us" (2004) 1 *Berkely Bus LJ* 1 8.

34 See parts 4 2 and 4 3 in Chapter 4.

35 *Williams v Inhabitants of Milton* 215 Mass 1 102 NE 355 (1913); *Frost v Thompson* 219 Mass 360 160 NE; *Navarro Savings Association v Lee* 446 US 458 (1980).

36 Theron (1991) *TSAR* 285.

37 Crane & Bromberg *Partnership* 174-176 (emphasis added).

In a more recent contribution on the subject[38] Olivier, together with Honiball, again examined this test and considered whether it is compatible with South African law.[39] While the test has not yet been directly applied in South Africa case law, the authors point to the matter of *Goodricke & Son (Pty) Ltd v Registrar of Deeds, Natal* ("*Goodricke*")[40] in support of their contention that trustee independence is a pre-requisite to establish a trust.

The facts of *Goodricke* were briefly that four natural persons entered into a deed of trust with the intention of creating a common investment fund. In terms thereof each undertook to pay a specified contribution into the trust fund which would in turn be applied for investments for the benefit of the trust fund.

The four founders were all both beneficiaries and trustees of the trust and in addition a juristic person ("the company") was co-opted as a fifth trustee to carry out the administration of the trust. The company's appointment as trustee could be terminated at any time by a bare majority of the remaining trustees, in which event the trustees could nominate one or more from their number to function in its place.[41]

The trustees undertook to apply the contributions paid into the trust fund to making a loan to a third party, which loan was to be secured by mortgage bond over certain immovable property registered in the name of the third party. However, the Registrar of Deeds declined to register the bond on the ground that, *inter alia*, the registration of the bond contravened the then still applicable section 54 of the Deeds Registries Act 47 of 1937, which did not allow for the registration of a bond in favour of a person acting as the agent of a principal.[42]

It was argued on behalf of the Registrar that the founders, being both trustees and beneficiaries, were in reality agents of one another and that the arrangement is really a partnership or joint venture for the mutual advantage of the four founders.[43] The court rejected this argument on the basis that the company had been appointed as a

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38 Honiball & Olivier *Taxation of Trusts* 253.

39 248-254.

40 1974 1 SA 404 (N).

41 *Goodricke & Son (Pty) Ltd v Registrar of Deeds, Natal* 1974 1 SA 404 (N) 405C-H.

42 407A-E.

43 409G-H.

fifth trustee and could only be removed by majority decision of the remaining trustees.[44]

Cameron et al describe *Goodricke* as "borderline on trustee independence" [45] and Honiball and Olivier interpret the reasoning therein to indicate that, had there been an absolute convergence of identity between trustees, a different conclusion would have been reached.[46] On this basis they suggest that, while the control test may not yet have been formally incorporated into South African jurisprudence, a similar decision will be reached when the substance-over-form principle is applied.[47]

Against this background, Honiball and Olivier submit that:

> "If in form the trustees have to act independently in the best interest of the beneficiaries, but in substance they are mere puppets in the hands of the beneficiaries, the substance of the agreement may well indicate that a partnership and not a trust was formed. Obviously, the other requirements for a valid partnership – namely that the object must be to make a profit, and that each party has to make a contribution to the undertaking and share in its profits – also have to be present. It is submitted that the mere fact that the express intention of the parties is to form a trust does not stand in the way of a court finding that in substance a partnership was formed.
>
> It may even be argued that any person who exercises a sufficient degree of control over a trustee may be held personally liable for trust debts on the basis that the substance of the agreement is that the trustee was his agent."[48]

This conclusion, it is submitted, is clearly premised upon the view that trustee independence is a pre-requisite to establish a valid trust. Honiball and Olivier's submission regarding the convergence of identity of the beneficiaries and trustees resonates in *Land Bank v Parker* where it was held that:

> "Though a trustee can also be a beneficiary, *the central notion is that the person entrusted with control exercises it on behalf of and in the interests of another*. This is why a sole trustee cannot also be the sole beneficiary: such a situation would embody an

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44 410B.

45 Cameron et al *Honoré* 92. See also B Wunsh "Trading and business trusts" (1986) 103 *SALJ* 561 564-6.

46 Honiball & Olivier *Taxation of Trusts* 253.

47 254.

48 254.

identity of interests that is inimical to the trust idea, and no trust would come into existence."[49]

It is on this basis, and the important principle of separation between control and benefit, that proponents of the establishment proposition may convincingly argue that a trustee's capacity for independence is a requirement for the establishment of a trust.

3 3 2 The fiduciary proposition

The proposition that trustee independence is a requirement to establish a trust is rejected by the principal advocates for the fiduciary proposition, PA Oliver, Strydom and Van den Berg.[50] In the predecessor of their work on trust law,[51] PA Oliver also rejects the suggestion by Honoré that "a degree of independence on the part of the trustee"[52] is an essential element of a trust as theoretically unsound.[53]

For these authors, the duty of a trustee to act independently stems from his fiduciary position. PA Olivier formulates this view in the following terms:

> "Honoré regverdig sy standpunt [that a degree of independence on the part of the trustee is an essential element for a trust] deur te sê dat 'n trustee nie in opdrag van iemand anders moet optree nie. Sy optrede moet deurgaans selfstandig wees.
>
> Alhoewel dit sekerlik belangrik is dat 'n trustee deurgaans selfstandig optree, *is dit 'n eienskap wat verband hou met die inhoud van die pligte wat op 'n trustee rus, voortspruitend uit die fidusiêre verhouding tussen hom en die begunstigde met betrekking tot die trustgoed.* Myns insiens kan *a degree of independence on the part of the trustee* nie as 'n essensiële element van 'n trust beskou word nie, maar eerder as 'n plig van 'n trustee om selfstandig en sonder inmenging van buite op te tree."[54]

Du Toit appears to support this view and argues that:

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49 *Land and Agricultural Bank of South Africa v Parker* 2005 2 SA 77 (SCA) para 19 (emphasis added).

50 Olivier et al *Trust Law and Practice* 2-14.

51 Published as a hardcopy. See Olivier *Trustreg* 36-37.

52 Honoré *The South African Law of Trusts* 5.

53 Olivier *Trustreg* 37.

54 37 (emphasis added). See also W Geach & J Yeats *Trusts: Law and Practice* (2007) 91 where it is suggested that a trustee is under a common law duty to act independently.

> "compliance with the duty of independence ensures commensurate compliance with one of the facets of a trustee's fiduciary duty."[55]

The establishment proposition, as advocated by L Olivier,[56] is also the subject of criticism from the proponents of the fiduciary proposition. PA Olivier et al express themselves in the following terms:

> "Prof L Olivier also believes that the requirement of independence is essential to the office of trustee. She is of the opinion that, if trustees are subject to an effective form of control (other than by the courts) by either the founder or the beneficiaries of the trusts, we not are dealing with a real trust institution, but rather with another legal phenomenon, such as agency. Such a decision by a court would, in our view, be attributable to the substance over form principle, rather than the essential elements of a trust.
>
> In our opinion, the abovementioned requirement of independence is an accessory to the office of trustee and merely an indication of how the trustee should behave in administering the trust. In our view, it relates to the contents of the trustee's duties. The essential elements of a trust relate to the basic concept of a trust, supplemented by the founder's trust object."[57]

The proposition that a trustee's duty of independence is rooted in his fiduciary position is echoed in *PPWAWU National Provident Fund v Chemical, Energy, Paper, Printing, Wood and Allied Workers Union (CEPPWAWU)* ("*PPWAWU*")[58] where Freund AJ drew a parallel between a trustee and a company director's duty of independence. In that matter the court was called upon to deal with the position of a trustee of a pension fund, or trustee in the broad sense, in relation to the beneficiaries of the fund.

Trustees in the broad sense must be distinguished from trustees in the narrow sense. A trustee in the narrow sense refers to those trustees of trusts defined in section 1 of the TPCA. Trustees that do not fall within this definition, but who nonetheless are entrusted with the affairs of others and consequently control property on behalf of others, have been described as falling within the ambit of

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55 Du Toit (2009) *THRHR* 642.

56 Theron (1991) *TSAR* 268 32; L Olivier "Trusts: traps and pitfalls" (2001) 118 *SALJ* 226.

57 Olivier et al *Trust Law and Practice* 2-14.

58 2008 2 SA 351 (W).

trustees in the broad sense.[59] It is self-evident that an examination of this second type of trust, despite not being subject to the provisions of the TPCA, can provide valuable perspectives on trusteeship in the strict or technical sense.[60]

PPWAWU concerned a battle between the applicant pension fund ("the fund") and the respondent trade union, CEPPWAWU, ("the trade union" or "union"). The fund was established by an earlier trade union, which later merged with other trade unions to form the respondent.

The fund was administered by a set of ten trustees, three of whom were appointed by the employers participating in the fund and the remaining seven by the respondent trade union.[61] Following from a string of resolutions adopted by the trustees of the fund, which attracted the displeasure of the trade union, the union adopted a resolution in terms of which those trustees appointed by it to the fund were required to obtain a mandate from the union in respect of all business conducted at the meeting of the fund's board of trustees and to act in accordance with such mandate.[62] The effect of this resolution was to compel the seven trustees appointed by the union to vote on the instructions of the union in fund matters.

At issue was the enforceability of the resolution made by the union. As a point of departure, the court held that the trustees of the fund owed a fiduciary duty to the fund, its members and other beneficiaries[63] and that, in terms of this fiduciary duty, they were required to exercise an independent judgement as to what constitutes the best interest of the fund.[64] In this respect, it was held that the applicable legal principles are the same as those that apply to a director of companies:[65]

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59 Examples of such trustees are trustees of pension funds and administrators of insolvent estates.

60 Du Toit (2009) *THRHR* 637.

61 *PPWAWU National Provident Fund v Chemical, Energy, Paper, Printing, Wood and Allied Workers Union* 2008 2 SA 351 (W) 354 F-I.

62 Para 2.

63 Para 20.

64 Para 25.

65 See *Fisheries Development Corporation of SA Ltd v Jorgensen; Fisheries Development Corporation of SA Ltd v AWJ Investments (Pty) Ltd* 1980 4 SA 156 (W) at 163D-G, where it was confirmed that a director of a company owes a duty toward to the company, and that in discharging that duty he is required to exercise an independent judgment.

> "The trustee's obligation to exercise an independent judgment, regardless of the views of the trade union (or employer) which appointed him, is analogous to the director's obligation to exercise an independent judgment, regardless of the views of any party which may have procured his or her appointment as a director."[66]

It accordingly followed that the resolution by the trade union requiring the trustees to act only in accordance with a mandate received from it, was contrary to law and unenforceable as this would obviate the exercise of independent discretion by the trustees in question.[67]

The conclusion arrived at in *PPWAWU*, that a trustee's duty of independence is a consequence of his fiduciary duty, is therefore in step with the theoretical basis for trustee independence advocated by the proponents of the fiduciary proposition.

It is submitted that the fiduciary proposition offers a sound theoretical basis for holding that trustees are required to exercise the control afforded to them over trust assets in an independent manner and that they are required to bring independent judgement to bear on the administration of the trust. However, as is elaborated below, the criticism of the establishment proposition by the proponents of the fiduciary proposition is misplaced.

3 4 The "independence duality"

The perception that the establishment and fiduciary propositions are incompatible is in my view attributable to a failure to recognise a duality in the broader concept of trustee independence. The recognition of this duality enables a reconciliation of the establishment and fiduciary propositions and reveals that each of these propositions offers a sound theoretical basis for a component of trustee independence.

For a trustee to act independently in the administration of trust affairs, two factors must be present. First, the trustee must be afforded the *capacity* to act independently by the trust deed. [68] Were a trustee has no independent power over the

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66 Para 27.

67 Para 42.

68 See E Cameron, M de Waal, B Wunsh, P Solomon & E Kahn *Honoré's South African Law of Trusts* 5 ed (2002) 262 where the authors state that:
"The trust instrument forms, as it were, the statute under which the trustee acts. Properly interpreted … it should be regarded as … 'objektiewe reg', though, of course, its source will be a valid contract, will, or other constitutive document."

administration of the trust, it follows that there can be no question of that trustee acting independently in the administration thereof.

Secondly, and where the aforesaid capacity is established, the trustee must *exercise* the capacity for independence. In instances where a trustee elects not to exercise the powers afforded independently, it can similarly not be said that the trust benefits from independent administration by the trustee.

This duality appears clearly from the facts of *Nel v Metequity* ("*Nel v Metequity*").[69] The respondents on appeal, two companies, Metequity Ltd ("Metequity") and Investec Business Services Ltd ("Investec Business Services"), were the trustees of the Jan Nel Bond Trust ("the trust"), a trust established in order to circumvent the provisions of the Participations Bonds Act 55 of 1981.[70]

In terms of the trust deed, the trust was established "for the purpose of providing an interest-bearing investment secured by mortgage of immovable property" advanced and settled upon trust. Practically, the founder, Metequity, paid R400 000 into trust, with the sum advanced to a third party, NWN Eiendome (Edms) Bpk ("NWN"). This loan was secured though a mortgage registered in favour of the trust over immovable property owned by NWN and the appellants bound themselves as sureties and co-principal debtors to the trust for the obligations of NWN.[71] Further, both trustees were subsidiaries of Metboard Ltd ("Metboard") and had no functions other than those in terms of the trust deed. The trust deed provided that for as long as Investec Business Services was a trustee, it alone would exercise and carry out the powers and duties of the trustees. In addition, the income of the trust, after deduction of expenses, was payable to the beneficiaries – being Metequity and to any person to whom it may have ceded its rights under the trust deed.[72]

This quotation has been replaced by a reference to *Land Bank v Parker* in the latest edition of this work. However, it is submitted that the characterisation of the trust deed as "objektiewe reg" remains sound. See also LI Coertze *Die Trust in die Romeins-Hollandse Reg* (1948) 87.

69 2007 3 SA 34 (SCA).

70 Para 7. The Participation Bonds Act 55 of 1981 provided certain formalities in the event of the granting of a participation bond, such as that the bond be registered in the name of a nominee company (section 2). The Collective Investment Schemes Control Act 45 of 2001 repealed the Act.

71 Para 2.

72 Para 6.

Upon default by NWN of its obligations to the trust, litigation ensued and, ultimately, the appellants were held liable based on the suretyships.[73]

The appellants contended that the trust was invalid on account of an identity of interests between the trustees and the beneficiary. This contention was based on two grounds. First, they contended that the object of the trustees was simply to generate income for Metboard which amounted to an impermissible identity of interests.[74] Secondly, that since the trustees are both subsidiaries of Metboard, had the same directors, made use of the same credit committee and appointed the same nominee to act on their behalf, the corporate veil should be lifted and the respondents treated as one entity.[75]

The appeal was dismissed, but not on the basis that an identity of interests in the sense referred to in *Land Bank v Parker* is permissible. Rather, in dealing with the main grounds advanced by the appellants, Streicher JA held that the fact that beneficiaries and trustees have identical interests insofar as the *object* of the trust is concerned, is immaterial. In this respect it was pointed out that an identity of interests will invariably exist in relation to the fulfilment of the trust object as both the trustees and beneficiaries have an interest in that effect be given to the trust deed. What was envisaged in *Land Bank v Parker* was an identity of interest in the same person.

Accordingly, the separate personalities of the corporate trustees, even where one is also a beneficiary, preclude an inimical identity from arising.[76]

Concerning the second ground, it was held that the mere fact that a company has only one shareholder who is in full control thereof does not constitute a basis for disregarding the company's separate juristic personality. What was required was for the appellants to show improper conduct on the part of the respondents in order to make out a case that the corporate veil should be lifted, which they had failed to do.[77]

The court's finding in relation to the question of identity of interest confirms that it is not the *possibility* of abuse that is determinative in whether a trust has been

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73 Para 3.

74 Para 9.

75 Para 10.

76 Para 9.

77 Paras 11-12.

established, but whether the trustees, objectively speaking, have the capacity to act independently. Where the two corporate trustees failed to bring an independent mind to bear upon the trust administration, this would in my view have constituted a fiduciary breach.

It is accordingly now clear that trustee independence has the two elements advocated for above, namely, the *capacity* for independent administration being afforded to the trustees, and the *exercise* of that capacity. If one or both factors are not present it cannot be suggested that a trustee is acting independently in the administration of the trust. These two factors may, for ease of reference, be labelled respectively "the capacity for independence" and the "exercise of independence".

The two factors are entirely distinct but connected to the broader principle of trustee independence and the establishment and fiduciary propositions each relates to only one aspect in turn. The establishment proposition succeeds in explaining the *capacity for independence* and the fiduciary proposition, it is submitted, relates to the question of the *exercise of independence*.

The distinct nature of each of these two factors means that the test in respect of establishing the presence of each is also distinct. The question whether a trustee is afforded the capacity to act independently is an objective test that stands to be determined with reference to the trust deed. The measure or type of independence that is required in this respect is examined in detail in Chapter 4,[78] but at this stage it bears emphasis that it is an objective question of law. The test for capacity for independence therefore evaluates the *de jure* status afforded to a trustee. In this respect, the key consideration is whether, objectively speaking, the trustee is afforded the capacity to act independently. This evaluation takes into account aspects such as the provisions of the trust deed, the wishes of the founder and the powers that have been afforded to a trustee, the beneficiaries or other third parties.[79] It is submitted that where a trustee has not been afforded the capacity to act

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78 See part 4 5 in Chapter 4.

79 For an example where the trustees were not provided sufficient capacity for independence see *Humansdorp Co-operative Ltd v Wait Humansdorp Co-operative Ltd v Wait* ECHC case no 2896/2012 of 1 November 2016. For a discussion of this case see part 6 4 3 in Chapter 6.

independently, the consequences are to be regulated with reference to the establishment proposition. [80]

In contrast, the determination of whether a trustee exercises independent control is a question of fact, and one that must be determined with reference to evidence relating to the particular trustee's factual conduct.

An evaluation of a trustee's conduct in this regard, therefore, focuses on the *de facto* administration of the trust. Accordingly, the question whether a trustee exercises the control entrusted to him in an independent manner requires a factual evaluation of the conduct of the trustee in question and particularly whether the trustee has brought independent judgement to bear upon the administration of the trust. Where a particular trustee, notwithstanding being afforded the capacity to act independently, fails to exercise such capacity, the consequences are regulated in terms of the fiduciary proposition.

It is against this background that the establishment and fiduciary propositions can, and should, be reconciled and, it is submitted, it is incorrect to label these two propositions as mutually exclusive or otherwise incompatible.

The harmony between these two propositions also emerges from a discussion by Van der Linde and Lombard regarding *Nel v Metequity*. In discussing whether the court ought to have invalidated the trust in *Nel v Metequity* on account of a lack of independence, the authors, in my view correctly, submit that:

> "The question can thus also be asked: 'How independent are the trustees?' Although the trustees and the beneficiary shared identical interests in so far as the object of the trust is concerned, the court held (par [9] 38E) that it does not constitute an identity of interests in the same person, purporting to act in a different capacity. In *casu*, the trustee acted for the benefit of the beneficiary and gave effect to the trust deed as it is their obligation to do (par [9] 38F). There were no indication to the court to point out any improper conduct in the establishment or use of the corporate respondents or in the conduct of their affairs (par [12] 39C). In other words, from a trust law point of view, they did not only *de iure*, but also *de facto*, acted independently. *De iure*, there are two corporate trustees with separate personalities. One of the trustees is also the sole beneficiary. The fact that they have the same directors *etcetera*, does not change the juridical situation. No indication

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80 See Honiball & Olivier *Taxation of Trusts* ch 10 for examples of how a founder may seek to limit the control that a trustee could exercise in the administration of a trust. This includes an over-prescriptive trust deed, the appointment of a protector or the conferring of powers of veto to beneficiaries.

was given that the *de facto* situation was any different. Although dealing with the scope of a redistribution order, the court in *Badenhorst*, laid down the following test (par [9] 260H-261B):

> 'To succeed in a claim that trust assets be included in the estate of one of the parties to a marriage, there needs to be evidence that such party controlled the trust and but for the trust would have acquired and owned the assets in his own name. Control must be *de facto* and not necessarily *de iure*.'

It is important, however, to note that such a situation *can* lend itself to misuse. Trustees have to be aware of the warning posed by the court in *Parker* (par [22] 87C-D), with regard to separation between control and enjoyment:

> 'The duties imposed on trustees, and the standard of care exacted of them derive from this principle. And it is separation that serves to secure diligence on the part of the trustee, since a lapse may be visited with action . . . The same separation tends to ensure independence of judgment on the part of the trustee – an indispensable requisite of office – as well as careful scrutiny of transactions designed to bind the trust . . .'"[81]

and

> "Trustees who do not exercise their powers independently run the risk of being held personally liable for breach of their fiduciary duty."[82]

Therefore, as long as the trustees are afforded the capacity for independent administration of the trust, it does not matter that there are risks that they would fail to exercise this capacity independently. Once such capacity is established, the establishment proposition holds that a valid trust is established (on condition that the other requirements for a trust are present) and questions regarding the failure of the trustees to act independently shift to be determined with reference to the principles underlying the fiduciary proposition. This principle is examined in further detail below.

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81 A van der Linde & S Lombard "Nel v Metequity Ltd 2007 3 SA 34 (SCA) – identity of interest between trustees and beneficiaries in so far as object of trust is concerned: effect on liability" (2007) 40 *De Jure* 429 435. The reference to "*Badenhorst*" is a reference to the matter of *Badenhorst v Badenhorst* 2006 2 255 (SCA). The reference to the "control test" in *Badenhorst* is examined in Chapter 4. See part 4 4 in Chapter 4.

82 436.

3 4 1 The establishment proposition as justification for the capacity for independence of trustees

As pointed out by Van der Linde and Lombard,[83] the "question on validity or not of a trust should be answered with reference to the *essentialia* of a trust".[84] Therefore, key to the acceptance of the establishment proposition as a theoretical basis for the capacity for independence is the question of whether trustee independence is an essential requirement for the validity of a trust.[85]

Trustee independence is not generally recognised as an essential requirement to establish a trust. The recognised requirements to establish a valid trust are:

(i) an intention on the part of the founder to create a trust;
(ii) the expression by the founder of the intention to create a trust in a mode suited to the creation of a legal obligation;
(iii) a reasonably certain definition of the trust property;
(iv) a reasonably certain definition of the trust object; and
(v) the lawfulness of the trust object.[86]

The fact that trustee independence is not traditionally recognised as an essential requirement for the validity of a trust suggests that the establishment proposition is inherently flawed. However, it may be argued that trustee independence is an indirect requirement for validity because it is implicit in the definition of a trust.

Du Toit et al explain that the creation of trust burdens the trustee to administer the trust property in accordance with the trust instrument's directives. It follows that trust provisions are by definition onerous in nature and that:

> "[f]or this reason, a trust founder must intend clearly and unambiguously to impose this burden on property through the creation of a trust in the strict sense".[87]

and

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83 435.

84 434. See also *Administrator's Estate Richards v Nichol* 1996 4 SA 253 (SCA).

85 Van der Linde & Lombard (2007) *De Jure* 429.

86 F du Toit, B Smith & A van der Linde *Fundamentals of South African Trust Law* (2019) 51; Cameron et al *Honoré* 136.

87 Du Toit et al *Fundamentals* 51.

> "What is therefore required is for the trust instrument to convey the founder's unequivocal intention to create a trust by imposing a binding trust obligation on the trustee or on another".[88]

The intention of the founder to create a trust is accordingly decisive. Du Toit et al elucidate:

> "A court adjudicating on an allegation that a trust is a sham must therefore determine whether all the creation requirements – and the intention requirement in particular – were met (in which case a trust was validly created) or whether the founder or the founder and trustee merely devised the appearance that these requirements were met (in which case no trust was created and the resultant arrangement constitutes a sham trust)."[89]

Due to the fact that the intention of the founder to create a trust is recognised as a requirement for the validity of a trust, the capacity for trustee independence may be imported as a requirement for validity if it is recognised that trustee independence is an essential element in the *definition* of a trust. Stated otherwise, if it were accepted that trustee independence is an essential characteristic of a trust, it follows that it is also an inherent requirement for the establishment thereof.

Trusts are, however, notoriously difficult to define.[90] As pointed out by De Waal:

> "In the most general sense a trust is an arrangement under which one person is bound to hold or administer property on behalf of another person or for an impersonal object and not for his own benefit. A trust in this sense would include, for example, persons such as tutors administering property for their pupils, curators of the mentally ill and agents holding property for their principals. But this will not do for a definition, because in this general sense all developed legal systems have the trust. And we know that is not true. Put differently, 'there is a difference between a law of entrusting and a law of trusts'."[91]

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88 52.

89 53.

90 DJ Hayton "Trusts" in DJ Hayton, SCJJ Kortman, AJM Nuytinck, AVM Stuycken & NED Faber (eds) *Vertrouwd met de Trust: Trust and Trust-like Arrangements* (1996) 3; T Honoré "Obstacles to the reception of trust law? The examples of South Africa and Scotland" in AM Rabello (ed) *Aequitas and Equity: Equity in Civil Law and Mixed Jurisdictions* (1997) 739, 794.

91 MJ de Waal "The core elements of the trust: aspects of the English, Scottish and South African trusts compared" (2000) 117 *SALJ* 548 548.

Accordingly, a definition of the trust must be more specific. Cameron et al suggest that a trust in the strict or narrow sense[92] arises when:

> "the creator or founder of the trust has handed over or is bound to hand over *to another the control of property* which is, or the proceeds of which are, to be administered or disposed of by the other (the trustee or administrator) for the benefit of some person other than the trustee as beneficiary, or for some impersonal object."[93]

This definition is echoed in article 2 of the Hague Convention on the Law Applicable to Trusts and on their Recognition:

> "For the purposes of this Convention, the term 'trust' refers to the legal relationships created – *inter vivos* or on death – by a person, the settlor, when assets have been placed under the control of a trustee for the benefit of a beneficiary or for a specified purpose." [94]

Each of these definitions emphasises the fact that the assets that form the subject matter of the trust must be placed under the control (Afrikaans: "*beheer*") of the trustee. The only notable exception is the definition contained in the TPCA where the term "control" is used only in the context of a so-called "*bewind* trust".[95]

The TPCA defines a trust in the following terms:

> "'trust' means the arrangement through which the ownership in property of one person is by virtue of a trust instrument made over or bequeathed –
>
> (a) to another person, the trustee, in whole or in part, to be administered or disposed of according to the provisions of the trust instrument for the benefit of the person

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92 As opposed to a trust in the broad sense.

93 Cameron et al *Honoré* 5 (emphasis added).

94 This convention is accessible on the website of the Hague Conference on Private International Law <http://www.hcch.net/index_en.php?act=conventions.text&cid=59> (accessed 25-01-2020) [emphasis supplied].

95 As explained in Chapter 2, South African law recognises the "*bewind* trust" where the trust estate is made over to the beneficiaries with the caveat that control is placed in the hands of another, the trustee, who is required to administer the estate for the benefit of the beneficiaries. See the text to n 125 in Chapter 2 and see also Cameron et al *Honoré* 10.

or class of persons designated in the trust instrument or for the achievement of the object stated in the trust instrument; or

(b) to the beneficiaries designated in the trust instrument, which property is placed under the control of another person, the trustee, to be administered or disposed of according to the provisions of the trust instrument for the benefit of the person or class of persons designated in the trust instrument or for the achievement of the object stated in the trust instrument,

but does not include the case where the property of another is to be administered by any person as executor, tutor or curator in terms of the provisions of the Administration of Estates Act, 1965 (Act No. 66 of 1965)".[96]

As appears from the above, a trust in the usual sense, as opposed to a *bewind* trust, is an arrangement where the ownership of property is made over to another who must administer it in terms of a trust deed. The only mention made of "control" in this definition is with reference to the *bewind* trust. In those circumstances, a trust can only exist where the property in question is placed under the control of the trustee notwithstanding the fact that ownership of the assets vests in the beneficiaries. It is therefore submitted that in the definition of a trust in the TPCA, the element of control must be understood as being implicit in the concept of ownership. In connection with this definition, Du Toit et al also correctly point out that:

"This definition of a trust in section 1 of the [TPCA] brings all trusts in the strict sense within the Act's regulatory ambit. Although the making over or bequeathing of the ownership in the trust property is central to the definition, it nevertheless provides that such ownership can vest in either the trustee or the trust beneficiaries. The Act thus confirms that a trustee's ownership of trust property is not the defining feature of the trust in the strict sense. The Act's definition of the trust instead identifies a trustee's administrative control, whether as owner or non-owner, as determinative of whether or not a trust in the strict sense is at hand."[97]

This construction is also consistent with the historical development of trusts and with other definitions of a trust,[98] such as that contained in section 1 of the Income Tax Act 58 of 1962:

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96 Section 1 of the TPCA (emphasis added).

97 Du Toit et al *Fundamentals* 7.

98 See part 2 2 in Chapter 2.

> "'Trust' means any trust fund consisting of cash or other assets which are administered and *controlled* by a person acting in a fiduciary capacity, where such person is appointed under a deed of trust or by agreement or under the will of a deceased person".[99]

Given the historical development of trusts discussed in Chapter 2,[100] it is submitted that a measure of control over the trust assets is an indispensable characteristic or element of a trust. In other words, the founder grants to the trustee administrative control over assets to be administered for the benefit of the beneficiary. The Oxford dictionary defines "control", when used as a transitive verb, as "to have control of, regulate; serve as control to check, verify". To be "in control" is defined as being "in charge" and "a controller" is "a person or thing that controls; person in charge of expenditure".[101]

In view of this definition, it is submitted that a trustee can only be "in control" of the trust estate when afforded the capacity to exercise the powers conferred by the trust deed, independently. It is axiomatic that where an individual acts upon instructions of another, he or she cannot be said to act independently. Accordingly, in order to be said to gain independence a trustee is to be afforded independent control over the administration of the trust. Where such independent control is absent, it is submitted the parties did not intend to create a trust, but rather a form of mandate or agency where either the founder or the beneficiaries retain ultimate control over the trust assets.

However, this argument was at one stage rejected by Honoré where he expressed the opinion that a trust may be valid notwithstanding the fact that the trustee may be subject to the control of the founder or the beneficiaries:

> "it is probably a mistake to require that for a valid trust the trustee must be independent of the control of the settlor or beneficiaries. Trusts which are terminable at the will of the sole beneficiary are certainly valid, as in the case of a trust whereby a nominee holds immovable property for a beneficiary (eg *Strydom v De Lange* 1970 (2) SA 6 (T)). In trusts of this sort the nominee may well be bound to obey the instructions of the

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99 Emphasis added. It is to be noted that this definition encompasses both trustees in a broad and a narrow sense. See *Commissioner for Inland Revenue v Friedman* 1993 1 SA 353 (A) 373F-374A.

100 See part 2 2 in Chapter 2.

101 W Branford (ed) *The South African Pocket Oxford Dictionary* (1987) 161.

> beneficiary as to the management of the property. Yet they are true trusts subject to the control of the court in regard to appointment and supervision (*Administrator Estate Cachalia v Dabhel Madressa Trust* 1940 WLD 14, *Ex Parte Thulsie* 1943 WLD 231, *Ex Parte Rajoo Dehal* 1937 WLD 136). Such a trust is distinguishable from mere agency by virtue of the fact that the trustee is *dominus* of the trust property and that the intention of the parties is to create a trust."[102]

Honoré, therefore, appears to suggest here that control by a trustee is *not* an essential element of the definition of a trust and that trusts in which the trustee does not have independent control over the assets remain valid. According to him the distinguishing factor between trusteeship and agency is the ownership (*dominium*) over the trust assets.

It is significant to note that the view expressed above is inconsistent with Honoré's later view on independence as set out in the third edition of his seminal work to the effect that a degree of trustee independence is required to found a trust.[103] Similarly, in the fourth edition of that work, Honoré and Cameron suggest that the legislative recognition of the *bewind* trust underscores an important principle that "control by the trustee/administrator rather than ownership is the essential feature of a trust".[104] Most recently, in 2008, Honoré has appeared to abandon his earlier view altogether when he wrote that:

> "It is true that trustees can be given a great deal of discretion as to how they invest trust funds and how they distribute income and capital among beneficiaries. This flexibility enables trusts to adapt to changing circumstances. But a trustee cannot be a mere tool of the settlor, subject to his orders as to the way in which he administers the trust."[105]

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102 T Honoré "Law of donations and trust" (1974) 7 *Ann Surv SA Law* 145 148.

103 Honoré *The South African Law of Trusts* 5.

104 T Honoré & E Cameron *Honoré's South African Law of Trusts* 4 ed (1992) 4. The specific quotation referred to above has been omitted from the fifth and sixth editions of this work by its subsequent authors. However, the principle that it is the control over the assets that is the essential feature of the trust is explicitly endorsed. See Cameron et al *Honoré* (2002) 7 and Cameron et al *Honoré* (2018) 8.

105 T Honoré "On fitting trusts into civil law jurisdictions" in Oxford Legal Studies Research Paper No. 27/2008 7 <https://papers.ssrn.com/sol3/papers.cfm?abstract_id=1270179> (accessed 04-08-2019).

This shift justifies the conclusion that independent control is an essential element of a trust. In addition, and as pointed out by L Olivier,[106] it is doubtful whether the cases cited by Honoré in support of his earlier view advance his argument since they all deal with the situation where the immovable property was registered in the name of a nominee.

It may also be submitted that Honoré's mention of the existence of a trust that may be terminable at the will of a beneficiary (such as in *Strydom v De Lange*[107]) as evidence for his view that a trustee may be under the control of a beneficiary is misplaced. The termination of the office of a trustee through his removal as such or the termination of the trust is conceptually distinct from his capacity to exercise independent administration of the trust while in office.[108]

It is notionally possible that a trustee may be removed at the direction of a beneficiary, but that such trustee would still have independent control over the administration of the trust while in office. The question of whether the trustee may succumb to threats of removal, or the termination of the trust, and thereupon fail to act independently, is in my view irrelevant for the purposes of the establishment proposition and is a question that must be considered in terms of the fiduciary proposition.

In view of the *dictum* in *Land Bank v Paker*, that the separation of control from benefit lies at the heart of the trust idea,[109] together with the accepted definition of a trust, it is submitted that the capacity for independent control by a trustee is (at least indirectly) an essential element to establish a trust. This is so because the capacity for independence is consistent with the central idea of a trust. Accordingly, where an asset is made over to another without granting such person the capacity to exercise independent control over such asset, there can be no suggestion of a trust being founded but that the construction is more akin to a mandate or agency.[110]

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106 Theron (1991) *TSAR* 268 286.

107 1970 2 SA 6 (T).

108 This distinction is highlighted by the distinction between "structural" and "asset" control discussed in Chapter 4. See the text to n 19 in Chapter 4.

109 2005 2 SA 77 (SCA) 86E-F.

110 The question regarding the measure and level of control required is examined in Chapter 4.

The establishment proposition, couched in terms of the independence duality, therefore provides a strong theoretical basis for explaining the consequences where a trustee is never afforded the capacity for independence, which explanation is not possible by way of the fiduciary proposition.

3 4 2 The fiduciary proposition as justification for the independent exercise of control

It is trite that a trustee is subject to a fiduciary obligation.[111] As pointed out by Heher JA in *Phillips v Fieldstone Africa (Pty) Ltd*,[112] "there is no magic to the term 'fiduciary duty'" and the essential requirement to establish such a duty is that one party must stand towards the other in a position of confidence and good faith which he is obliged to protect.[113]

It is a trustee's fiduciary relationship *vis-à-vis* the founder and beneficiaries that forms the axis around which the administration of the trust turns. As Olivier et al put it:

> "[t]he practical implementation of a trustee's duties within the ambit of the fiduciary relationship can be said to provide the electric current which ensures proper and enduring light for the trust."[114]

This fiduciary duty has found legislative expression in section 9 of the TPCA, which requires a trustee to act in the performance of his duties and the exercise of his powers "with the care, diligence and skill which can reasonably be expected of a person who manages the affairs of another".[115]

It is further uncontroversial to suggest that this duty to act in a manner that can reasonably be expected of a person who manages the affairs of another includes the

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111 *Sackville West v Nourse* 1925 AD 516 533; *Doyle v Board of Executors* 1999 2 SA 805 (C) 813A; De Waal (2000) *SALJ* 557; Cameron et al *Honoré* 13.

112 2004 3 SA 465 (SCA) 159.

113 159G. The theoretical basis for a trustee's fiduciary duty is examined in Chapter 5. See also *Robinson v Randfontein Estate Gold Mining Co Ltd* 1921 AD 168.

114 Olivier et al *Trust Law* 2-3.

115 Section 9 of the TCPA.

duty to act independently.[116] This simple, but important, principle was expressed over a century ago by Bristow J in the following terms:

> "A trustee should be wholly independent, he should regard equally the interests of all the creditors, and he should be in position to carry out his duties without fear, favour or prejudice, in the interest of all the various creditors."[117]

The proposition that a duty of independence forms part of a trustee's broader fiduciary duty has found judicial[118] as well as academic[119] support and, considering the aforementioned, there can in my view no longer be any serious debate on the issue.

The fiduciary proposition further succeeds to explain the obligation of a trustee to exercise independent discretion in the management of trust affairs in a manner that the establishment proposition is unable to do.

Recognition of the independence duality therefore permits for the establishment and fiduciary propositions to be reconciled. The manner in which these two propositions interrelate is accurately captured by Van der Linde and Lombard as follows:

> "Facts and circumstances can show that there is no *de iure* separation between control and enjoyment in that the trustees and beneficiaries are the same resulting in such a trust being invalid. It is also possible that there can be *de iure* separation in the sense that there is in fact an independent trustee, but *de facto* separation is lacking due to the way the trust is administered. In such an instance it seems that the trust can be valid (in that the *essentialia* are objectively met) but that trustees can be liable for breach of trust, trust

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116 *Fisheries Development Corporation of SA Ltd v Jorgensen; Fisheries Development Corporation of SA Ltd v AWJ Investments (Pty) Ltd* 1980 4 SA 156 (W) 163D-G.

117 *Goldseller v Hill* 1908 TS 822 835. This matter related to the position of a trustee of an insolvent estate and thus refers to a trustee in the broad sense. However, it is submitted that the principle that a person who manages the affairs of another should remain independent is also directly applicable to a trust in the narrow sense. See *Hoppen v Shub* 1987 3 SA 201 (C) 217C; *Tjimstra NO v Blunt Mackenzie NO* 2002 1 SA 459 (T) 474E-F; *African Bank Ltd v Weiner* 2003 4 All SA 50 (C) 54B-C.

118 *PPWAWU National Provident Fund v Chemical, Energy, Paper, Printing, Wood and Allied Workers Union (CEPPWAWU)* 2008 2 SA 351 (W).

119 F du Toit "The fiduciary office of a trustee and the protection of contingent trust beneficiaries" (2007) 18 *Stell LR* 469; Du Toit (2009) *THRHR* 637.

assets can be taken in consideration for purposes of a redistribution order, or trustees can be held to the provisions of the trust deed."[120]

3 4 3 "Developing non-independence" and the "curtailment of capacity for independence"

The recognition of the independence duality is further confirmed as accurate when the issue of "developing non-independence" and "curtailment of capacity" is considered.

"Developing non-independence" refers to the gradual decline in trustee independence through a progressive failure by the trustees to exercise their capacity for independence.

It is conceivable that trustees of a trust be afforded the capacity for independence at the trust's inception, and also initially exercise such independence. However, where the exercise of independence is eroded through time (owing to, for example, a growing familiarity between the trustees and founder), a situation may arise where it can no longer be said that the trust is being administered independently.

In terms of the establishment proposition, the existence of a trust will be placed in doubt where a trustee is not afforded the requisite capacity for independence. However, the evaluation of the trustee's independence is, under this model, confined to the time of establishing the trust. It is at this point in time that the trustee either has the requisite capacity for independence, thus giving rise to a trust, or not, thereby not giving rise to a trust.

Where trustee independence is gradually eroded, it is in my view theoretically and practically unsound to suggest that the trust's existence is compromised. The correct position is that a failure by a trustee to exercise the capacity for independence constitutes a breach of fiduciary duty. Therefore, developing non-independence may give rise to a claim for the breach of trust and the possible removal of the trustee.

Trustee independence may also be compromised by an attempt to "curtail capacity for independence" through a proposed amendment to the trust deed. It is, however, submitted that such an attempted amendment will be visited with nullity by virtue of the provisions of section 9(2) of the TPCA. In terms of the independence duality model, a trust is established if, initially, a trustee is afforded sufficient capacity

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120 Van der Linde & Lombard (2007) *De Jure* 438.

for independence. Once so established a trustee has a fiduciary obligation to exercise such capacity independently. Any amendment that would divest a trustee of the capacity for independence (and consequently excuse a trustee from such obligation on account of impossibility) would in my view not invalidate the trust, but would itself be void by virtue of the provisions of section 9(2).

That section, which follows the statutory duty of a trustee to act in a manner that can be "expected of a person who manages the affairs of another",[121] reads as follows:

> "Any provision contained in a trust instrument shall be void in so far as it would have the effect of exempting a trustee from or indemnifying him against liability for breach of trust where he fails to show the degree of care, diligence and skill as required in subsection (1)."[122]

Therefore, once it is accepted that a trustee has a fiduciary responsibility to act independently, it follows that, by virtue of the provisions of section 9(2) of the TPCA, any provision inserted in a trust deed that is aimed at somehow curtailing this duty, would be void for having the effect of exempting or indemnifying a trustee against liability for failing to act independently.

The fiduciary proposition, couched in terms of the independence duality, therefore provides a sound theoretical and academic explanation for "the developing independence" and "curtailment of capacity" conundrums, which cannot be achieved through the establishment proposition alone.

3 5 Conclusion

As the discussion above reveals, the establishment and fiduciary propositions are not mutually exclusive but are, in reality, complementary. They each relate to one aspect of the independence duality, which requires a distinction to be drawn between the capacity of trustees to act independently and their exercise of that capacity.

Put differently, where trustees have no objective *de jure* capacity to make trust decisions independently from third parties (such as the founder, beneficiaries, or advisers), it cannot be said that a trust has been established.

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121 Section 9(1) of the TCPA.

122 Section 9(1).

However, once the requisite objective measure of independence is met (this measure is examined in the following chapter) the investigation turns to the manner in which the trustees in question have exercised this capacity. Where a trustee fails to bring an independent mind to bear upon the administration of the trust, such failure constitutes a breach of the trustee's fiduciary duty in accordance with the fiduciary proposition. Such a breach would not invalidate the trust but could give rise to a claim in the hands of the beneficiaries.

Viewed in this light, it is clear that the principal propositions explored in this dissertation both explain one aspect of the "independence duality". In the following chapters, these two propositions will be further examined. In particular, the question is asked what measure of capacity for independence on the part of the trustees is required for a trust to be valid. In addition, competing propositions regarding the requirement that this capacity is to be exercised independently are examined. In this regard, it is submitted that the duty to bring an independent mind to bear upon trust business flows from the trustees' fiduciary duty.

The development of these propositions in this manner establishes, it is submitted, a sound theoretical framework to further examine questions regarding so-called "sham" trusts as well as under what circumstances it would be open to a court to disregard the trust's separate estate.

CHAPTER 4: THE ESTABLISHMENT PROPOSITION

4 1 Introduction

In the preceding chapter, the interplay between the establishment proposition and the independence duality was briefly explored. The establishment proposition holds that, first and foremost, a founder must intend to establish a *trust*, and then also that a trustee's capacity for independent control of the trust estate is a pre-requisite for the establishment of a trust.

It, however, remains altogether uncertain what *type* and *degree* of control is required to satisfy this pre-requisite. In this chapter, this question is considered against the backdrop of the so-called "control test" primarily developed and applied in the USA. The examination of this test, together with its constituent aspects of "structural" and "asset" control, provide a basis to consider the type and extent of control required by the establishment proposition.

4 2 The control test

The control test is a product of judicial development in the USA[1] and ascribes liability for corporate conduct to the true controllers of a juristic entity or collective. The test has its origins in the context of partnerships and in particular in the context of joint-stock companies.[2]

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1 *Williams v Inhabitants of Milton* 215 Mass 1 102 NE 355 (1913); *Frost v Thompson* 219 Mass 360 160 NE; *Navarro Savings Association v Lee* 446 US 458 (1980).

2 As explained in Chapter 3, the description "joint-stock company" can be misleading. Depending on the jurisdiction, a joint-stock company does not constitute a corporation but a partnership. The joint-stock company has its roots in the conventional partnership where each partner brings into the partnership capital or skill. However, where the capital funding requirement is much larger, necessitating a greater number of partners, a structure developed whereby the parties delegated management authority to a smaller number (that is, a management committee). Accordingly, the joint-stock company has been defined as "an association in which the capital is thrown into one mass employed for the general benefit, each member participating in the gain according to the proportion of stock or capital which belongs to him." W Wait *A Treatise Upon Some of the General Principles of the Law: Whether Legal, or of an Equitable Nature, Including Their Relations and Application to Actions and Defences in General, Whether in Courts of Common Law, Or Courts of Equity; and Equally Adapted to Courts Governed by Codes* IV (1885) 159.

During the mid-1980s the Canadian academic, Robert Flannigan, made a strenuous attempt to demonstrate that the control test also applied to trusts in the Anglo-Canadian context.[3] Flannigan proposed that the beneficiaries of a trust may be held liable for the debts of the trust estate in circumstances where they were the effective controllers of the trust business. He, therefore, suggested that the "limited liability"[4] that is afforded to beneficiaries of a trust should be deemed lost in circumstances where such beneficiaries are in a position to control the administration of the trust.[5] This thesis supports the notion of an agency relationship between trustee and beneficiary (in terms of which the beneficiary is liable for the debts of the trust estate) on the basis of policy considerations.[6]

In the USA the control test is primarily employed to distinguish between trusts and partnerships. This distinction is illustrated in *Hecht v Malley* ("*Hecht*")[7] where the United States ("US") Supreme Court held as follows:

> "The 'Massachusetts Trust' is a form of business organization, common in that state, consisting essentially of an arrangement whereby property is conveyed to trustees, in accordance with the terms of an instrument of trust, to be held and managed for the benefit of such persons as may from time to time be the holders of transferable certificates issued by the trustees showing the shares into which the beneficial interest in the property is divided. These certificates, which resemble certificates for shares of stock in a corporation and are issued and transferred in like manner, entitle the holders to share ratably in the income of the property, and, upon termination of the trust, in the proceeds.
>
> Under the Massachusetts decisions, these trust instruments are held to create either pure trusts or partnerships, according to the way in which the trustees are to conduct the affairs committed to their charge. If they are the principals and are free from the control of the certificate holders in the management of the property, a trust is created; but if the certificate holders are associated together in the control of the property as principals and

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3 RDM Flannigan "Beneficiary liability in business trusts" (1984) 6 *Est & Tr Q* 278; RDM Flannigan "The control test of principal status applied to business trusts: Part I" (1986) 8 *Est & Tr Q* 37; RDM Flannigan "The control test of principal status applied to business trusts: Part II" (1986) 8 *Est & Tr Q* 97.

4 This limited liability should not be equated to the limited liability afforded to shareholders of a juristic person, but refers to the protection from creditors of the trust estate established through the mechanism of separate estates examined in Chapter 2.

5 Flannigan (1984) *Est & Tr Q* 278.

6 These policy considerations are discussed in further detail below.

7 265 US 144 (1924).

> the trustees are merely their managing agents, a partnership relation between the certificate holders is created."[8]

Flannigan approaches the matter from the perspective of the public good. He argues that the imposition of a similar control test to trusts outside the USA (notably in Canada) would serve to deter the true decision makers from harmful risk-taking, shielding third parties from harmful risk and thereby augmenting the public good.[9] If actors who enjoy effective control over the administration of an estate also enjoy immunity from claims by third parties, so the argument goes, the probabilities of such actors acting in a manner prejudicial to third parties are amplified.

However, where the effective controllers are held liable for the consequences of their actions, the risk of such liability serves as an effective bulwark against the administration of an estate in a manner which may prejudice third parties. Flannigan phrases the argument as follows:

> "The rationale for the business trust control test is the same as that for the limited partnership control test. Beneficiaries (like limited partners) bear a different liability exposure than do trustees. If their different risk aversion can be applied to the employment of trust assets that risk aversion will affect third parties. But third parties are never required to submit to a limited liability risk aversion in persons whom they actually deal with unless they agree. They are not subject to limited liability in persons who contract with them either directly or through an agent. In order to maintain this principle of personal liability for personal conduct the beneficiaries must be prevented from affecting the trust assets which are the security for third parties. Accordingly, the ability to affect trust assets is the factor which establishes whether the trustee or the beneficiary is liable to third parties."[10]

and

> "Generally, if risk-taking is not regulated, if it is insulated from its own consequences, it is more likely to involve the taking of greater risks and to result in a higher probability of loss

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8 146-147 (emphasis added). See also *Navarro Savings Association v Lee* 446 US 458 (1980).

9 Flannigan (1986) *Est & Tr Q* 97 111; Flannigan (1984) *Est & Tr Q* 278. See also Comment (1928) 37 *Yale LJ* 1103 1111-1112.

10 Flannigan (1984) *Est & Tr Q* 278 284.

to third parties. This rationale is as applicable to partial control as it is to complete superior control."[11]

Flannigan's proposals were heavily criticised by Maurice Cullity.[12] For Cullity, the imposition of liability on beneficiaries (or trustees) must be based on the *intention* of the parties to the trust and not on the basis of control.[13] He contended that, outside of the USA and in particular within the Anglo-Canadian context, there was no justification for the imposition of liability on the basis of Flannigan's risk-aversion principle.[14]

This disagreement resulted in a vigorous academic debate between Flannigan and Cullity that culminated in Cullity's final academic article on the issue in 1996.[15] The debate now appears to have been settled and, as discussed below, Cullity's view is to be preferred. This view is also compatible with the establishment proposition and the central tenet of the independence duality.

The imposition of a control test on trusts, as proposed by Flannigan, is therefore not supported. However, the work done by Flannigan and others[16] in unpacking the control test is valuable in understanding the establishment proposition and, in particular, the question of the type and measure of control required thereunder.

Particularly helpful is the distinction between "structural" and "asset" control developed by Flannigan.[17]

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11 Flannigan (1986) *Est & Tr Q* 97 111.

12 MC Cullity "Liability of beneficiaries – a rejoinder" (1985) 6 *Est & Tr Q* 35; Flannigan (1986) *Est & Tr Q* 37; MC Cullity "Liability of beneficiaries – a further rejoinder" (1986) 8 *Est & Tr Q* 130.

13 Cullity (1985) *Est & Tr Q* 35 42.

14 51.

15 See, Flannigan (1984) *Est & Tr Q* 278; Cullity (1985) *Est & Tr Q* 35; Flannigan (1986) *Est & Tr Q* 37; Flannigan (1986) *Est & Tr Q* 97 111; Cullity (1986) *Est & Tr Q* 130; RDM Flannigan "'Control' and the control basis of legal relationships and business organizations" (1989) 53 *Sask L Rev* 1; RDM Flannigan "Trust or agency: beneficiary liability and the wise old birds" in S Goldstein (ed) *Equity and Contemporary Legal Developments* (1990) Ch 4 and MC Cullity "Personal liability of trustees and rights of indemnification" (1996) 16 *Est & Tr* J 115.

16 See, Comment (1928) 37 *Yale LJ* 1103; M Honiball & L Olivier *The Taxation of Trusts in South Africa* (2009) and L Olivier "Trusts: traps and pitfalls" (2001) 118 *SALJ* 224 227.

17 Flannigan (1986) *Est & Tr Q* 37.

"Structural control", on the one hand, refers to the ability to regulate the *manner* in which the trust is administered. The structure of the trust relates to, for example, the composition of the body of the trustees, arrangements regarding voting, notice of meetings, quorum requirements, and reporting to beneficiaries.[18] Control over the structure of the trust may be granted to trustees (or others) by vesting them with the power to appoint and remove trustees, fill trustee vacancies, or amend the trust deed. These powers, when exercised, determine the structural framework of the trust. Persons with such powers are said to have "structural control" over the trust.

"Asset control", on the other hand, refers to the ability to regulate the business of the trust.[19] Typically this type of control entails the power to determine the manner in which trust assets are employed and is said to be "the highest authority capable of being exercised in relation to any particular aspect of the actual business operation".[20] Examples of asset control are the power to alienate, invest, disburse or otherwise encumber trust property.

In summary, structural control refers to control over the framework through which the trust assets are managed and asset control refers to the direct control over the trust assets through the framework set by the trust deed.

4 3 The development of the control test through the cases

The first hint of what would later develop into the control test appears in the English case of *Smith v Anderson* ("*Smith*").[21] In that matter, a trust deed provided for the purchase by the trustees of shares in the capital stock of different submarine telegraph companies.

The proposed venture was capital intensive, and a scheme was developed whereby capital could be raised by permitting investors to subscribe in the trust against payment. These investors would, in turn, be furnished with transferable certificates.[22]

The trust deed at issue provided that the income accruing from the submarine shares (together with any proceeds from the sale thereof) was to be applied by the

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18 41.

19 39.

20 39.

21 *Smith v Anderson* (1880) 15 ChD 247 (CA).

22 274.

trustees in three distinct ways: first, by paying 6% interest on the certificates issued to subscribers; secondly, by redeeming these trust certificates at an agreed price of £120; and, finally, when all the certificates had been redeemed, the surplus, if any, was to be divided between the former certificate holders.[23] The trustees accordingly had limited powers to sell securities and reinvest but had more extensive powers if their decision was confirmed at a meeting of certificate holders. Smith, who was a certificate holder, sought relief declaring the scheme illegal by virtue of the provisions of the then applicable Companies Act of 1862 (requiring registration of an association with more than 20 members that intended to conduct business).

At issue, therefore, was whether this arrangement constituted an association or whether a trust was established, in which event registration under the Companies Act of 1862 was not required. In the court *a quo* Smith was successful, but the decision was overturned on appeal.

It was held in the Court of Appeal that the arrangement constituted a trust and not an association or partnership. This conclusion was partially reached on the ground that there was no evidence that the trustees were agents of the certificate holders:

> "They [the parties to the scheme] are from the first entire strangers who have entered into no contract whatever with each other, nor has either of them entered into any contract with the trustees or any trustee on behalf of the other, there being *nothing in the deed pointing to any mandate or delegation of authority to anybody to act for the certificate holders as between themselves*, and nothing, as it appears to me, by which any liability could ever be cast upon the certificate holders either as between themselves or between themselves and anybody else. Therefore, I cannot arrive at the conclusion that the certificate holders form an association within the meaning of this Act of Parliament any more than persons who subscribe for debentures in a railway … Persons who have no mutual rights or obligations do not, according to my view, constitute an association because they happen to have a common interest or several interests in something that is to be divided between them."[24]

Smith informed the decision in *Williams v Inhabitants of Milton* ("*Milton*"),[25] a case often credited as being the first in which the control test was applied to trusts in the

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23 274.

24 274-275 (emphasis added).

25 215 Mass 1 102 NE 355 (1913).

USA.[26] That matter turned on the proper interpretation and status of the Boston Personal Property Trust ("the Boston Trust") and in particular on how it stood to be taxed.

The Boston Trust was a property-holding trust with immovable assets held in different tax jurisdictions. The trust also issued transferable certificates to beneficiaries and the proceeds of the trust's business would ultimately flow into the hands of these certificate holders.[27]

In the city of Boston, taxes in respect of the trust property had been assessed on the basis that the trust was, in reality, a partnership (in the sense of the joint-stock company) whereas in the municipalities of Milton, Waltham, and Brookline the trust property was taxed as property held in trust, the income of which was payable to another.[28]

After discussing *Smith*, and analysing the trust deed in question, the court held that the trustees had sufficient control over the trust assets for the arrangement to constitute a trust. The court held:

> "The certificate holders are throughout called '*cestuis que trustent.*' The certificate holders, or *'cestuis que trustent,'* are in no way associated together, nor is there any provision in the indenture of trust for any meeting to be held by them. The only act which (under the trust indenture) they can do is to consent to an alteration or amendment of the trust created by the indenture or to a termination of it before the time fixed in the deed. *But they cannot force the trustees to make such alteration, amendment or termination. It is for the trustees to decide whether they will do any one of these things*. All that the certificate holders or *'cestuis que trustent'* can do is to give or withhold their consent to the trustees taking such action.
>
> And the giving or withholding of consent by the *cestuis que trust* is not to be had in a meeting, but *is* to be given by them individually. As we have said, no meeting of the *cestuis que trust* for that or any other purpose is provided for in the trust indenture. The trustees of the Boston Personal Property Trust have a right to sell the trust securities and reinvest the proceeds, and also a limited power to borrow on the security of the trust property. The certificate holders, or '*cestuis que trustent,'* as they are called in the trust deed, have a common interest in precisely the same sense that the members of a class of life tenants (among whom the income of a trust fund is to be distributed) have a

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26 Although the *Milton* case is generally credited with originating the control test, it had been used before. See, PLW "Liability of shareholders in a business trust – the control test" (1962) 48 *Va L Rev* 1105 and the cases cited there in the text to n 1 and n 12.

27 356.

28 356.

> common interest, but they are not *socii*, *and it is the trustees, not the certificate holders, who are the masters of the trust property*.
>
> The sole right of the *cestuis que trust* is to have the property administered in their interest by the trustees, *who are the masters*, to receive income while the trust lasts, and their share of the corpus when it comes to an end."[29]

Therefore, the control over the manner in which the trust property was to be applied was held to be definitive of the status of the trustees and, as a consequence, the nature of the arrangement. From the *ratio* above, it is clear that the court in *Milton* considered asset control as decisive in this regard, as it was the control over the assets and not the structure in terms of which the trust was administered, that was determinative. Consequently, the nature of the Boston Trust as a trust was affirmed and it stood to be taxed on that basis.

In *Frost v Thompson* ("*Frost*"),[30] decided by the same court only a year after the *Milton* case, the degree of certificate holder control was again held to be decisive, but increased emphasis was placed on structural control. That matter concerned efforts of the holder of a promissory note to execute the note against the assets of a joint-stock company, the Buena Vista Fruit Company.

The plaintiff had previously brought a successful action against the trustees in their personal capacity which he sought to enforce. The action in question related to the trustees' right to be indemnified from the trust estate. In affirming the test set out in the *Milton* case, the court held as follows:

> "A declaration of trust or other instrument providing for the holding of property by trustees for the benefit of the owners of assignable certificates representing the beneficial interest in the property may create a trust or it may create a partnership. Whether it is the one or the other depends upon the way in which the trustees are to conduct the affairs committed to their charge. If they act as principals and are free from the control of the certificate holders, a trust is created; but if they are subject to the control of the certificate holders, it is a partnership."[31]

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29 *Williams v Inhabitants of Milton* 215 Mass 1 102 NE 355 (1913) 358 (emphasis added).

30 219 Mass 360 160 NE 1009 (1914).

31 365.

In examining the declaration of trust in question, the court arrived at the conclusion that the association was a partnership based on the level of structural control enjoyed by the certificate holders:

> "Tested by the principles laid down [in the *Milton* case], the Buena Vista Fruit Company is a partnership and not a trust. It is a voluntary association organized under two instruments, one called a 'declaration of trust' and the other, 'by-laws.' These two instruments provide that the shareholders representing two thirds in value of outstanding shares have power to remove either or all of the trustees at any time, without assigning any cause, and to appoint others to fill the vacancy; to terminate the trust at any time earlier than that limited for its duration in the declaration of trust, and to terminate it by requiring conveyance of the property to other trustees upon new trusts, or to a corporation. A majority of the shareholders at any time by vote may amend the declaration of trust. The by-laws may be 'altered, amended or repealed' by vote of the majority of the shareholders 'at any annual or special meeting of the … shareholders.' These provisions demonstrate that this association is a partnership and not a trust."[32]

Subsequent case law in the USA has supported the analysis in the *Frost* case when similar powers were reserved for beneficial owners.[33] It thus appears that structural control has been placed on a level footing with asset control as an indicator of the type of control required to establish a trust.

However, in the minority opinion by Blackmun J in the US Supreme Court case of *Navarro Savings Association v Lee* ("*Navarro*")[34] some doubt was cast on the suitability of structural control as a test for independence.

In *Navarro*, the respondents were the eight trustees of Fidelity Mortgage Investors ("Fidelity"), a business trust organised in terms of the laws of Massachusetts. Significantly, the trust deed vested the trustees with full asset control over the trust assets.[35] During 1971, the trustees lent a sum of $850 000 to a Texas firm in return

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32 365-366.

33 See *First Nat'l Bank v Chartier* 305 Mass 316 25 NE 2d 733 (1940); *Neville v Gifford* 242 Mass 124 136 NE 160 (1922).

34 446 US 458 (1980).

35 459. The deed provided that the trustees held title to the real estate investments of the trust for the benefit of the beneficiaries (termed shareholders) and that they had exclusive authority over the property "free from any power and control of the Shareholders, to the same extent as if the Trustees were the sole owners of the Trust estate in their own right …"

for a promissory note payable to them. The note was secured by an undertaking from Navarro Savings Association ("the Association") (the petitioner in the appeal) to cover the obligations of the Texas firm to the trustees.[36] The trustees were all resident in the state of Massachusetts, but the residence of the various shareholders (numbering approximately 990) varied, with at least some being resident within the state of Texas.[37]

In 1973, the trustees called upon the Association to perform in terms of the undertaking and, when the Association refused, enforcement action in a federal court followed.[38] The Association objected to the court's jurisdiction on the basis that the parties lacked sufficient diversity of residence.[39] The district court concluded that a business trust was a citizen of every state in which its shareholders reside and that, since some shareholders were residents of the state of Texas, the parties lacked the required diversity of residence to confer jurisdiction onto the federal court system.[40]

An appeal to the United States Court of Appeals for the Fifth Circuit reversed the finding of the district court on the basis that Fidelity's residence was to be

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36 *Navarro Savings Association v Lee* 446 US 458 (1980) 459.

37 460.

38 Due to its federal nature, there are two parallel court systems in the USA, namely state and federal courts. State and local courts are established by a state (within states there are also local courts that are established by cities, counties, and other municipalities). Federal courts are established under the US Constitution to decide disputes involving the Constitution and laws passed by congress. State courts have broad jurisdiction limited by geographical area. Federal court jurisdiction, by contrast, is limited to the types of cases listed in the Constitution. These include cases against the federal government, matters involving the interpretation of the Constitution or laws of congress, bankruptcy and patents, and disputes between citizens of differing states based on the "diversity principle" (see the text in n 39 below). For a useful explanation of the US legal system see <http://www.uscourts.gov/about-federal-courts/court-role-and-structure> (accessed 11-07-2018).

39 In the matter of *Strawbridge v Curtis* 7 US 267 (1806), the US Supreme Court set out the basis of jurisdiction of federal courts on the diversity principle. According to this principle, a federal district court would have jurisdiction over a matter if there is complete diversity of residence between the parties. The principle was laid down that for diversity jurisdiction to exist, no party on the one side of a suit may be a citizen of the same state as a party on the other side of the suit. Therefore, if, in the event of a multiple parties, one of the claimants was a citizen of the same state as one of the defendants, the matter should be dealt with by the State Court of the state concerned.

40 *Navarro Savings Association v Lee* 446 US 458 (1980) 460.

adjudicated with reference to those of the trustees and not the shareholders. In arriving at this conclusion the Court of Appeals relied on the asset control enjoyed by the trustees.[41] The court therefore held that, since diversity of residence existed between the trustees on the one hand (who were residents of Massachusetts), and the Association on the other (which was a resident of Texas), the federal courts enjoyed jurisdiction to hear the matter.

The US Supreme Court granted *certiorari*[42] and affirmed the finding of the Court of Appeals. The court held that Fidelity's residence should be determined based on that of its trustees. In the justification, the majority per Powell J, relied on the earlier decision in *Bullard v Cisco*,[43] and on the control that the trustees enjoyed over the trust's *assets*. The position was set out as follows:

> "Bullard reaffirms that a trustee is a real party to the controversy for purposes of diversity jurisdiction when he possesses certain customary powers to hold, manage, and dispose of assets for the benefit of others. The trustees in this case have such powers. At all relevant times, Fidelity operated under a declaration of trust that authorized the trustees to take legal title to trust assets, to invest those assets for the benefit of the shareholders, and to sue and be sued in their capacity as trustees."[44]

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41 460.

42 "Certiorari" may be translated from Latin as "to be informed of, or to be made certain in regard to". See, <http://www.techlawjournal.com/glossary/legal/certiorari.htm> (accessed 11-07-2018). According to the Legal Information Institute of Cornell University, "Certiorari is most commonly associated with the writ that the Supreme Court of the United States issues to review a lower court's judgment. A case cannot, as a matter of right, be appealed to the US Supreme Court; therefore, a party seeking to appeal from a lower court decision may file a petition to a higher court for a writ of certiorari. That writ is the formal order to the lower court to deliver its record of the case for review. In the US Supreme Court, if four Justices agree to review the case, then the Court grants certiorari (often abbreviated as "cert."); if that does not happen, the Court denies certiorari" <https://www.law.cornell.edu/wex/certiorari> (accessed 11-07-2018).

43 290 US 179 189 (1933) 190. In *Bullard v Cisco* the trust beneficiaries were numerous investors who had conveyed bonds to a central committee. The agreement in terms of which the bonds were so conveyed, did not use trust terminology, but it was nevertheless held that the power enjoyed by the committee over the assets of the beneficiaries rendered them the relevant persons for litigation and that "[t]he beneficiaries were not necessary parties and their citizenship was immaterial". *Bullard v Cisco* therefore affirmed juristic asset control as the determinative measure of control.

44 *Navarro Savings Association v Lee* 446 US 458 (1980) 464.

The asset control enjoyed by the trustees was accordingly held to be determinative of the nature of the trust. Since the nature of the trust was affirmed, the trust's residence was determined with reference to that of the trustees and, consequently, sufficient jurisdictional diversity existed for the Federal Courts to exercise jurisdiction.

In a dissenting opinion, Blackmun J disagreed strongly with the conclusion reached by the majority of the court. He affirmed the control test as applied in *Frost* and, in an implicit endorsement of the view that structural control is central to the control test, opined as follows:

> "That the trustees' control over the assets of Fidelity is substantial may be accepted without quarrel. The Court fails to recognize, however, that the Declaration of Trust [applicable to Fidelity] lodges in the beneficial shareholders substantial control over the actions of these trustees. Article 2.1 of the Declaration provides that the trustees are to be elected at annual shareholder meetings by a majority of the shares voted… Article 2.2 provides that trustees may be removed from office, with or without cause, by vote of the majority of the outstanding shares… Article 6.7 vests in the shareholders two significant powers: the ability to call a special meeting upon the request of not less than 20% of the outstanding shares, and the requirement that any sale, lease, exchange, or other disposition of more than 50% of the trust assets is to be made only upon the affirmative approval of the holders of a majority of the shares … Most significantly, Art. 8.2 reserves to the holders of a majority of the shares the right to terminate the trust at any shareholder meeting, and Art. 8.3 gives them the power to amend the Declaration of Trust itself."[45]

and

> "While I prefer and accept the Court of Appeals' approach to this case, I am persuaded, on that approach, that one cannot ignore the pervasive measure of control that Fidelity's shareholders possess over the trustees' actions taken [on] their behalf. … That factor, in my view, is the principal distinction between the ongoing business entity at issue here and the trust relationship among certificate holders and the bondholders' committee that was at issue in Bullard v Cisco 290 U.S. 179 (1933), cited and relied upon by the Court … Though the question is not free from doubt, in the light of these circumstances I believe that the citizenship of Fidelity should be determined according to the citizenship of its beneficial shareholders, and that diversity jurisdiction does not exist in this case."[46]

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45 469.

46 476.

Notwithstanding the debate regarding the relevance of structural control in determining the true controllers of the trust, *Navarro* affirmed the control test as the decisive manner in evaluating the nature of a trust-like arrangement in the USA.

The decision in *Navarro* has given rise to significant debate. *Carden v Arkoma Associates* ("*Carden*"),[47] a matter in which the US Supreme Court was called upon to determine the residence of a limited partnership, appeared to overturn *Navarro*'s reliance on the control test in the context of an association.

Carden concerned a limited partnership organised in terms of Arizona law. The association, Arkoma Associates ("Arkoma"), had both general and limited partners and sued the defendants who were citizens of Louisiana, in a federal court. One of the limited partners was a resident of Louisiana and the defendants accordingly contended that the court lacked jurisdiction on the diversity principle.[48]

The matter proceeded to trial and Arkoma succeeded. Upon appeal by the defendants, the Fifth Circuit affirmed the decision of the court *a quo* holding that Arkoma's residence was to be determined based on its general partners only.[49]

This decision was overruled on appeal to the US Supreme Court. Arkoma repeated the argument that its residence should be determined based on its general partners as these were the persons who had effective control over the partnership. In support it cited *Navarro*.[50] The US Supreme Court distinguished *Navarro* on the basis that "*Navarro* had nothing to do with the citizenship of the 'trust,' since it was a suit by the trustees in their own names."[51]

The court held that for the purposes of an association, which it stressed was not a corporate entity, the residence of all partners was relevant. In this regard, it relied on the so-called "doctrinal wall" of *Chapman v Barney*,[52] a case involving a joint-stock company and to the effect that the US courts would only treat incorporated groups of "artificial entities" as legal persons and would assimilate all other groupings to partnerships.[53]

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47 494 US 185 (1990).

48 186.

49 186.

50 199.

51 192 to 193.

52 129 US 677 (1889).

53 *Puerto Rico v Russell & Co* 288 US 476 (1933) 480.

There matters laid in abeyance for over a decade and a half. In 2016, the US Supreme Court decided the matter of *Americold Realty Trust v ConAgra Foods Inc* ("*Americold*").[54]

Americold involved a lawsuit brought by several corporations against the owner of an underground warehouse, housing the corporations' food products. The warehouse, and its content, were destroyed by fire in 1991 and the corporations sought to hold the owner, Americold Realty Trust ("Americold"), liable for their loss.[55] Americold was a so-called real estate investment trust ("REIT") created under Maryland law.

Initially, the suit was brought in a Kansas state court but was later transferred to a federal district court.[56] On appeal, the appellate court raised the issue of Americold's residence for jurisdictional purposes. It was clear that the plaintiff corporations were all residents of different States but the appellate court concluded, on the basis of *Carden*, that Americold's residence was to be determined by that of its shareholders.[57] Since there was no evidence before the court on the residence of all of Americold's shareholders, so it was held, the parties failed to demonstrate the residence diversity required to establish jurisdiction.[58]

The US Supreme Court affirmed this finding. In so doing, it singled out for discussion Americold's argument that, under *Navarro*, "anything called a 'trust' possesses the citizenship of its trustees alone, not its shareholder beneficiaries as well." In distinguishing *Navarro*, the Court first examined the nature of a REIT. In Maryland a real estate investment trust (REIT) is defined as an "unincorporated business trust or association" in which property is held and managed "for the benefit and profit of any person who may become a shareholder".[59]

Against this background, the Supreme Court observed that "[a]s with joint-stock companies and partnerships, shareholders [in a REIT] have 'ownership interests'

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54 577 US 136 *S Ct* 1012 (2016).

55 Para I.

56 Para I.

57 See *ConAgra Foods Inc v Americold Logistics LLC* 776 F. 3d 1175 1182 (2015) 1180-1181. The terms "beneficiaries" and "shareholders" were used interchangeably or conjunctively as "beneficiary shareholders".

58 Para III.

59 Maryland Corporations & Associations Code (2014) paras 1-704(b)(5), 8-101(d).

and votes in the trust by virtue of their 'shares of beneficial interest'."[60] It is therefore clear that, for the Supreme Court, the measure of asset control afforded to shareholders of a REIT distinguished it from a "traditional trust" and placed it on equal footing with joint-stock companies and partnerships.[61]

The distinction between "traditional trusts", as was the focus in *Navarro*, and a REIT such as Americold, was determinative. In this regard the Supreme Court held that:

> "Traditionally, a trust was not considered a distinct legal entity, but a 'fiduciary relationship' between multiple people… Such a relationship was not a thing that could be haled into court; legal proceedings involving a trust were brought by or against the trustees in their own name … And when a trustee files a lawsuit or is sued in her own name, her citizenship is all that matters for diversity purposes… For a traditional trust, therefore, there is no need to determine its membership, as would be true if the trust, as an entity, were sued.
>
> Many States, however, have applied the 'trust' label to a variety of unincorporated entities that have little in common with this traditional template. Maryland, for example, treats a real estate investment trust as a 'separate legal entity' that itself can sue or be sued… So long as such an entity is unincorporated, we apply our 'oft-repeated rule' that it possesses the citizenship of all its members … But neither this rule nor Navarro limits an entity's membership to its trustees just because the entity happens to call itself a trust.
>
> We therefore decline to apply the same rule to an unincorporated entity sued in its organizational name that applies to a human trustee sued in her personal name."[62]

The significance of the distinction between a REIT and a "traditional trust" in interpreting *Americold*, was underscored in *Wang, by and through Wong v New Mighty U.S. Trust* ("*New Mighty*").[63] *New Mighty* concerned a rags-to-riches tale of a family patriarch and the subsequent feud over the sequestering of his immense wealth to the exclusion of his wife.

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60 Para II. The reference to the "ownership interest" and votes according to "shares of beneficial interest" appears from the Md. Corp. & Assns. Code Ann. Paras 8-7049(b)(5) and 8-101(d).

61 See also MS McNamara and RCK Boyd "REIT citizenship and the impact of *Americold Realty Trust* on jurisdictional challenges" <https://www.pillsburylaw.com/en/news-and-insights/reit-citizenship-and-the-impact-of-americold-realty-trust-on.htm> (accessed 01-05-2018).

62 Para III.

63 843 F.3d 487 (2016).

Born into a poor tea-farming family in Taiwan in 1917, Yung-Ching Wang ("Yung-Ching"), who was unable to attend high school as a result of poverty, married the teenage Yueh-Lan Wang ("Yueh-Lan") in 1935. In 1954 he established the Formosa Plastics Group. This group achieved tremendous success and, by the time of Yung-Ching's death in 2008, *Forbes* magazine ranked him as the 178th wealthiest person in the world, with an estimated net worth of $6.8 billion.[64]

Although Yung-Ching remained married to Yueh-Lan through the course of his life, he also fathered several children with two other women, Wang Yan Chiao ("Chiao") and PC Lee ("Lee"). Yueh-Lan helped raise some of these children and she considered one child in particular, Winston Wen-Young Wong ("Winston"), whose biological mother was Chiao, as her son.

Three years prior to his death, Yung-Ching made several distributions and stock transfers to the New Mighty US Trust ("the US Trust"), a trust formed under the laws of the District of Columbia in the USA, and thereby effectively placed the bulk of his wealth out of the reach of Yueh-Lan.[65] In October 2010, Winston, who purported to act on behalf of Yueh-Lan, sued the US Trust for return of the distributions made to it.[66]

One of the issues that stood to be determined was whether the court had jurisdiction to hear the matter. The matter came before the district court prior to the hearing of *Americold* and, in employing *Carden*'s language of an "artificial entity", the court concluded that the residence of a traditional trust was also to be determined by that of its beneficiaries. The composition of the US Trust's beneficiaries was such that diversity of jurisdiction would have been excluded.

An appeal to the Court of Appeals for the District of Columbia Circuit followed but was held in abeyance by the passing of Yueh-Lan and interlocutory disputes about Winston's authority to proceed with the action. This dispute was referred to the

64 Para I.

65 Para I.

66 Winston alleged that Lee and members of her family created the New Mighty Trust to defraud Yueh-Lan and that the distributions to this trust resulted from undue influence that Lee exerted on Yung-Ching. See *Wang, by and through Wong v New Mighty U.S. Trust* 843 F.3d 487 (2016) n 5.

appellate court to be heard together with the appeal but was again delayed when it became apparent that the US Supreme Court was to determine *Americold*.[67]

The Court of Appeal consequently had the benefit of the Supreme Court's ruling in *Americold* and, on the basis of the distinction between a REIT and a "traditional trust" raised in that case, it concluded that the residence of a traditional trust was to be determined by that of the trustees.[68]

What remained to be determined was whether the US Trust was, in fact, a "traditional trust". In considering this question the court placed considerable emphasis on Title 19 of the DC Code, which includes the District of Columbia's version of the Uniform Trust Code.[69]

The court concluded that "a traditional trust was a trust that lacks juridical person status."[70] In arriving at this conclusion the court highlighted sections of the DC Code and the Restatement of Trusts[71] that emphasise "control" as a central feature of a trust. It held: "[a] trustee shall take reasonable steps to take *control* of and protect the trust property"[72] and "[t]he trustee is under a duty to the beneficiary to take reasonable steps to take and keep *control* of the trust property".[73]

Against this background, the US Trust was held to be a traditional trust and the decision of the court *a quo* was reversed. The questions regarding Winston's authority to proceed with the action were referred to the district court for consideration.[74]

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67 Para I, n 6.

68 13.

69 District of Columbia Code para 19-1304.01(2).

70 16-17.

71 The restatement on trusts is a product of the American Law Institute ("ALI"). The ALI is an independent organisation based in the USA that states as its aim the production of "scholarly works to clarify, modernize, and improve the law". See the website of the ALI at <https://www.ali.org/about-ali/> (accessed 11-07-2018).

72 District of Columbia Code para 19-1308.09 (emphasis added).

73 Restatement (second) of trusts, para 175 (emphasis added).

74 Page 20. The litigation in the matter is ongoing. After the resolution of litigation relating to the appointment of the executors in Taiwan, the US Trust raised a motion that litigation in the USA be halted on the basis of *forum non conveniens*. This defence was determined in favour of the US Trust by the district court in February 2018. An appeal followed to the United States Court of Appeal for the District of Columbia, see *Robert Shi, as executors of the will of Yueh-Lan Wang et al v New Mighty US Trust et al* 18-

Navarro, *Americold* and *New Mighty* all illustrate that control by the trustees (and by implication the control test as developed in *Milton* and *Frost*) remains an important consideration in the USA for determining the true nature of a trust and in particular whether it is a "traditional trust", which in turn affects the question of liability.

4 4 The control test in South Africa

In the South African context, the control test often solicits a reference to the reasoning in *Badenhorst v Badenhorst* ("*Badenhorst*").[75]

In that case, the SCA approached the question of whether assets of a trust are to be taken into account for a redistribution order in a divorce, in terms of section 7(3) of the Divorce Act 70 of 1979 ("the Divorce Act")[76] on the basis of control exercised by one of the parties.

The matter entailed a bitter divorce wherein Mrs Badenhorst contended that the assets of a family trust were to be taken into account as part of Mr Badenhorst's estate for the purposes of calculating a possible redistribution of assets following their divorce. The facts were briefly as follows.

The parties were married to each other out of community of property in 1981, and subsequently lived on the family farm, at that stage, owned by Mr Badenhorst's father. It was at all times understood that Mr Badenhorst would eventually inherit his

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7066 (D.C. Cir. 2019) available at <https://www.courtlistener.com/opinion/4600239/robert-shi-v-new-mighty-us-trust/> (accessed 21-01-2020). The court of appeal held that the district court erred in upholding the plea of *forum non conveniens* and, again, remitted the matter to the district court for consideration on the merits. At the time of writing (December 2019) the matter remained unresolved.

75 2006 2 SA 255 (SCA). See BS Smith "Sham trusts in South Africa: *tempora mutantur, nos et mutamur in illis* (times change, and we change with them)" (2019) 136 *SALJ* 550 556; F du Toit, B Smith & A van der Linde *Fundamentals of South African Trust Law* (2019) 140-141.

76 The power of a court to order a redistribution under this Act is examined in detail in part 6 5 2 in Chapter 6. For present purposes, it is sufficient to note that section 7(3) of the Divorce Act is aimed at ameliorating an inequity that may arise in a divorce where the parties at the time of their marriage did not have the option of concluding a marriage out of community of property with the inclusion of the accrual system, which option was only introduced in 1984.

father's farm and the couple farmed the farm as if it were already theirs. Upon the death of Mr Badenhorst's mother, the farm devolved upon a trust, where it was held at the time of the trial. In addition, the couple established another trust, the Jubli Trust in which they, during the currency of their marriage, acquired immovable property for investment and recreation.[77] It was the status of this trust that formed the focus of the appeal.

In 2001 Mr Badenhorst purchased the shares in a company, Catwalk Investments (Pty) Ltd, in the name of the Jubli Trust. The company owned the franchise for the Seeff Real Estate Agency for the area where the parties lived. While 50% of the shares in the company were donated to Mrs Badenhorst, the trust retained the other 50%.[78]

The Jubli Trust was founded by Mr Badenhorst's father and the trustees were Mr Badenhorst and his brother, and the capital beneficiaries were Mr Badenhorst's children. Mrs Badenhorst was an income beneficiary.[79]

Mr Badenhorst also enjoyed structural control over the trust. In this sense he had the right to discharge his co-trustee at will and appoint another in his place, and the trust deed provided that its terms could only be varied with the consent of the founder and, upon his death, that of his children. The trust deed also provided that Mr Badenhorst was to be compensated from the trust estate for his duties as trustee.[80]

The evidence in the trial revealed that Mr Badenhorst ignored the core principles of the proper administration of the trusts. Combrinck AJA summarised his conduct as follows:

> "From the evidence of [Mrs Badenhorst] it is clear that in his conduct of the affairs of the trust [Mr Badenhorst] seldom consulted or sought the approval of his co-trustee, his brother. He was, in short, in full control of the trust. Furthermore, he paid scant regard to the difference between trust assets and his own assets. So, for instance, in a written application for credit facilities with the local co-operative, dated 27 March 2002, he listed the trust assets as his own. The liabilities in the form of bonds over the fixed property and the rental income from the buildings he also described as his. At one stage he insured the

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77 *Badenhorst v Badenhorst* 2006 2 SA 255 (SCA) para 4.

78 Para 4.

79 Para 10.

80 Para 10.

> beach cottage (a trust asset) in his own name. A property in Calitzdorp registered in [Mr Badenhorst's] name … was financed by the trust. He received an income of R50 000 a month from the Seeff agencies when in fact the shares (50%) in the company Catwalk Investments (Pty) Ltd were owned by the trust. It is evident that, but for the trust, ownership in all the assets would have vested in [Mr Badenhorst]."[81]

It is therefore clear that, on the facts, Mr Badenhorst utilised the trust assets as his own. In holding that these assets were to be included in his estate for the purposes of the divorce action, the court adopted a "but for" test[82] in the sense that it examined whether the above amounted to evidence that Mr Badenhorst "controlled the trust and but for the trust would have acquired and owned the assets in his own name".[83] It is within this context that the control exercised by Mr Badenhorst was emphasised.

> "Control must be *de facto* and not necessarily *de iure*. A nominee of a sole shareholder may have *de iure* control of the affairs of the company but the *de facto* control rests with the shareholder. *De iure* control of a trust is in the hands of the trustees but very often the founder in business or family trusts appoints close relatives or friends who are either supine or do the bidding of their appointer. *De facto* the founder controls the trust. To determine whether a party has such control it is necessary to first have regard to the terms of the trust deed, and secondly to consider the evidence of how the affairs of the trust were conducted during the marriage."[84]

It is therefore immediately clear that the court, in *Badenhorst*, did not employ the traditional control test as developed in the USA to determine whether a trust was established. The validity of the trust was assumed. What was in question was whether, based on Mr Badenhorst's conduct, the "veneer of the trust" was to be "pierced".[85]

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81 Para 11.

82 This is the phrase preferred by Du Toit: F du Toit "Trusts and the patrimonial consequences of divorce: recent developments in South Africa" (2015) 8 *Journal of Civil Law Studies* 665 699. See also M de Jong, J le Roux-Bouwer & T Manthwa "Attacking trusts upon divorce and in maintenance matters: guidelines for the road ahead (1)" (2017) 80 *THRHR* 201 n 33 206. However, the phrase is criticised as not meaningful as all trustees hold property "but for" the trust: Smith (2019) *SALJ* 565.

83 Para 9.

84 Para 9.

85 For the reasons set out in Chapter 6, I am of the view that this terminology is to be avoided. A more accurate term for the relief at hand is, in my view, "disregarding the separate estate" of the trust. See part 6 2 in Chapter 6. There is some debate regarding

Smith also accurately points out that the terminology used in *Badenhorst* is inaccurate:

> "the requirement that control must be 'de facto *and not necessarily* de iure' is also potentially misleading. It is most certainly beyond cavil that a trustee *must* have de iure control of the trust property. However, the context in which this remark was made is all-important. Combrinck AJA clearly had in mind de facto 'control' *by a dominant trustee* that results in *an abuse* of the trust form. But even so, the requirement that such control need '*not necessarily* [be] *de iure*' is inaccurate because it implies that abuse which is the result of de iure control could lead to a piercing of the trust's veneer."[86]

Smith proceeds to explain, in my view correctly, that the terminology used in *Badenhorst* is more appropriate in the context of examining the validity of the trust, as the retention of control by the founder might have compromised the establishment of the trust.[87] For this reason, the "control test" formulated in *Badenhorst* cannot be equated with the control test as developed in the USA, which has not been applied in South Africa.

Honiball and Olivier have advocated for what they also refer to as a "control test" to be applied to trusts in South Africa.[88] They have suggested that where the founder of a trust exercises effective control over the trust, through for example an over-prescriptive trust deed, the validity of the trust may be compromised.[89]

In support of this submission, the authors point to so-called "section 38 trusts" established in accordance with section 38(2)(b) of the (now repealed) Companies Act 61 of 1973 ("the 1973 Act").[90] Section 38 of the 1973 Act prohibited financial

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whether the court in *Badenhorst* did in fact disregard the separate estate of the Jubli Trust or whether it simply ordered redistribution in terms of section 7(3) of the Divorce Act. As discussed in Chapter 6, I agree with Smith that *Badenhorst* was an instance where the trust's separate estate was disregarded. See the discussion at part 6 5 2 in Chapter 6.

86 Smith (2019) *SALJ* 565.

87 565.

88 The central tenet of Honiball and Olivier's thesis is examined in Chapter 3. See the text to n 38 in Chapter 3.

89 Honiball & Olivier *Taxation of Trusts* 250-251; Olivier (2001) *SALJ* 224 227.

90 The 1973 Companies Act has since been replaced by the Companies Act 71 of 2008 (the "2008 Act").

assistance by a company for the purchase of its own shares.[91] However, section 38(2) provided an exception to this general rule, and allowed a company to give financial assistance for the purchase of its own shares if the shares were to be held in trust for the benefit of its employees.[92]

A study by L Olivier[93] revealed that the deeds of trusts so established often afford special powers to the company *vis-à-vis* the trustees, such as the power to:

(i) appoint and remove trustees;
(ii) fix trustees' remuneration and to determine the interest rate on loans made to or incurred by the trust;
(iii) amend the trust deed and even terminate the trust; and
(iv) decide who should be beneficiaries, which shares can be allocated to which beneficiaries and how payments should be made.[94]

These powers are plainly structural in nature. Other examples listed by Honiball and Olivier them, are a mix of asset and structural control.[95] It accordingly appears

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91 Although the 1973 Act has now been repealed, many such trusts are still in existence today. In addition, there is reason to believe that this practice will continue under the new 2008 Act. While section 38 of the 1973 Act has not been duplicated in the 2008 Act, it is submitted that the spirit of section 38(2) of the 1973 Act finds expression in section 44(3) of the 2008 Act. Section 44(3) of the 2008 Act allows a company to provide financial assistance for the purchase of its own shares if such assistance is directed at existing employees, or a particular category of potential recipients. It appears that these provisions are aimed at aiding South African corporations to transform their shareholder base and contribute to the policy of Black Economic Empowerment. Despite the fact that section 44 of the 2008 Act does not require financial assistance to be held in trust, as was the case under section 38 of the 1973 Act, it is submitted that the practice of establishing empowerment trusts, as well as the familiarity of section 38 trusts, will contribute thereto that financial assistance in terms of section 44 of the 2008 Act will often be conducted through the trust institution.

92 Section 38(2)(b) of the 1973 Act.

93 Olivier (2001) *SALJ* 224.

94 227.

95 Examples listed by them are:
(i) that the founder retains the lifetime power to dismiss and appoint trustees and to vary the provisions of the trust deed;
(ii) that the founder is entitled to a distribution of trust capital or income in his or her capacity as the founder;

that Honiball and Olivier do not emphasise the distinction between asset and structural control and that the decisive factor for validity is that the founder be divested of general control over the trust assets and that a functional separation between the control over and benefit of those assets be established. If the founder retains control over the trust estate, Honiball and Oliver contend that the validity of the trust may be compromised.[96]

This result represents a significant departure from the control test proposed by Flannigan. Flannigan does not propose that control by others renders the trust invalid, but merely seeks to impose liability on such controllers for the consequences of acts by the trustees.

The "control test" proposed by Honiball and Olivier is therefore reminiscent of the establishment proposition, which differs from the US control test in important respects.

4 4 1 The establishment proposition and the control test distinguished

The chief distinction between the control test and the establishment proposition is its goal or objective. The control test seeks to justify liability of the true controllers of the trust based on the risk-aversion principle. Flannigan explains the application of the principle as follows:

> "Risk-taking is implemented through what has been described herein as asset control. An ability to make decisions in relation to the employment of assets gives effect to a person's risk set or risk-taking. The regulation of risk-taking, accordingly, is accomplished by the establishment of a rule that attaches principal status to a person who is in a position to apply his risk set to the employment of assets. This prevents others being exposed to what would be an unregulated, and hence objectionable, risk-taking. Typically, this means that the person now labelled as a principal will be liable for a loss to third parties. If a third party suffers loss, it will be because the business operation has generated a tort or degenerated into insolvency. When a beneficiary has an ability to affect the employment of assets (*i.e.*, a right to control), his risk set will have been incorporated into the

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(iii) that the trustees must at all times act in the exclusive interests of the founder; and
(iv) that important administrative decisions require the founder's prior written consent.
See Honiball & Olivier *Taxation of Trusts* 250.

96 Honiball & Olivier *Taxation of Trusts* 248-254.

operation and he will be partly responsible for the probability of tort and contract loss that is associated with that operation."[97]

The control test, therefore, has a utilitarian goal and seeks to militate against the abuse of the trust form and to ensure responsible management of the trust. In order to achieve this goal, the test is flexible in the sense that it not only focusses on the position of the trustees but also examines the level (and type) of control enjoyed by others.

The control test is also not tied to application at a specific point of time. It does not matter that the control over the management of the trust is granted to others when the trust is established or at any point thereafter. Where trust decisions are in practice made by persons other than the trustees, the control test holds that those persons should be held responsible for the consequence of those decisions.

The establishment proposition, on the other hand, does not purport to have any such utilitarian goal or equitable effect. The sole purpose of this proposition is to unmask other arrangements, such as mandate or agency, masquerading as a trust.

This is achieved by focussing on the type and measure of control enjoyed by the trustees at the time of the establishment of the trust. Once it is established that there is a sufficient degree of separation of control and benefit in the sense suggested in *Land Bank v Parker*[98] when the trust is established, the establishment proposition ceases to be relevant.

Any further considerations of the exercise of control after the establishment of the trust must then be determined with reference to the fiduciary proposition as the other constituent part of the independence duality.

4 4 2 The control test not applicable in South Africa

As discussed above, Flannigan's control test was the subject of a spirited academic debate between him and Cullity, who opposed its implementation.[99] Cullity opposed the implementation of the control test on the basis that there was no

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97 Flannigan (1986) *Est & T Q* 111.

98 2005 2 SA 77 (SCA) para 19.

99 Cullity (1985) *Est Tr Q* 35. The debate between Flannigan and Cullity on this issue has dissipated and it is submitted that the issue has now become settled in favour of Cullity. See Flannigan (1989) *Sask L Rev* 1 and Cullity (1996) *Est & Tr J* 115.

theoretical justification for the imposition of an agency relationship without the parties thereto agreeing. In support he referenced *Garnac Grain Co Inc v HMF Faure & Fairclough Ltd*:[100]

> "The relationship of principal and agent can only be established by the consent of the principal and the agent. They will be held to have consented if they have agreed to what amounts in law to such a relationship, even if they do not recognize it themselves and even if they have professed to disclaim it …"[101]

Cullity concludes that the proposition that an agency relationship may be imputed based solely on the control exercised by a beneficiary "is not warranted in principle or … on the authorities".[102]

Cullity's criticism of the importation of Flannigan's control test holds equally from a South African perspective. It is trite that agreement or ratification by the principal is a pre-requisite for the establishment of an agency relationship. Silke stated the principle as follows:

> "Generally, the principal gives, and the agent accepts, a prior authorization or instruction to do the act or series of acts, but such prior authorization or instruction by the principal is not essential because the principal may ratify and adopt acts done on his behalf by the agent without authority; such subsequent ratification is equivalent to authority given *nunc pro tunc*."[103]

and

> "The contract of agency is created by the express or implied assent of the principal and agent. Where there is no intention to create the relationship of principal and agent there can be no contract of agency."[104]

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100 [1968] AC 1130 (HL).

101 1137. Discussed in Cullity (1985) *Est & Tr Q* 51.

102 52.

103 JM Silke *The Law of Agency in South Africa* 3 ed (1981) 38.

104 81. See also *Smale v Castle Wine & Brandy Co* 1936 CPD 213; *Ocean Cargo Line Ltd v F R Waring (Pty) Ltd* 1963 4 SA 641 (A).

An agreement of sorts on the part of the principal is accordingly a pre-requisite for the imposition of an agency relationship and Flannigan's control test is therefore incompatible with South African law also on the same basis as argued by Cullity in the Canadian context.

However, there is a further (arguably more significant) reason why the agency relationship is incompatible with the underpinning of a South African trust.

Notwithstanding his criticism of the control test, Cullity does not object to the application of an agency relationship to a trust:

> "There is, of course, no reason why trust and agency relationships cannot coincide and they often are intended to do so, particularly in the case of bare trusts where the trustee acts solely at the direction of the beneficiaries."[105]

and

> "It is quite clear that in many situations trustees will also be agents. This occurs, for example, in the familiar case of investments held by an investment dealer as nominee or in the case of land held by a nominee corporation. In such cases, the trust relationship that arises by virtue of the separation of legal and equitable ownership is often described as a bare trust and for tax and some other purposes it is quite understandably ignored.
>
> The distinguishing characteristic of the bare trust is that the trustee has no independent powers, discretions or responsibilities. His only responsibility is to *carry out the instructions of his principals – the beneficiaries*. If he does not have to accept instructions, if he has any significant independent powers or responsibilities, he is not a bare trustee and it seems clear that … the relationship is to be treated as a trust."[106]

In as far as this view may refer only to a trust in the broad sense, there can be no cause for disagreement. However, where it refers to a trustee in the narrow sense,[107] it cannot be supported. It is also reminiscent of a similar comment by Honoré made in 1974, which has been disagreed with in Chapter 3.[108]

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105 Cullity (1996) *Est & Tr J* 138.

106 Cullity (1985) *Est & Tr Q* 36 (emphasis added).

107 This distinction is discussed in detail in Chapter 3. See the text below n 57 in Chapter 3.

108 T Honoré "Law of donations and trusts" (1974) 7 *Ann Surv S African L* 145 148. Honoré's comment is discussed in Chapter 3, but reproduced here for sake of convenience:

The establishment proposition, founded in the independence duality, requires that trustees be afforded the capacity for independent control and where such capacity is not provided for, it cannot be said that the parties intended to establish a trust.

The incompatibility of agency and trusts may be explained based on trusteeship constituting an office. Cameron captured this distinction accurately in the following terms:

> "Honoré has accorded this formality its clearest doctrinal authority, distinguishing throughout his work between 'trust' in the wide sense, and 'trust' in the strict or narrow sense. The former exists 'whenever a person is bound to hold or administer property on behalf of another or for some impersonal object and not for his own benefit', and may include office-holders such as tutors, curators and executors, as well as agents, who do not hold office. The 'special feature' of a trust in the strict sense, by contrast, is that the trustee 'acts not in his private but in an official capacity other than one of the nominate capacities referred to above'.
>
> Trusteeship, then, is a 'quasi-public office', in the performance of which the trustee is subject to judicial scrutiny and to the supervision of the Master of the Supreme Court. In this it is distinct from agency, even though the agent undoubtedly owes fiduciary duties to the principal. It is also distinct however from curatorship, executorship and tutorship in the duties it imposes and the powers it accords."[109]

Therefore, the emphasis that South African law places on trusteeship as an office, means that the trust form is incompatible with an agency relationship and where the parties have agreed (perhaps tacitly) that the "trustee" would be the agent of his principal (irrespective of whether it is the "founder" or "beneficiary"), it is submitted

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> "it is probably a mistake to require that for a valid trust the trustee must be independent of the control of the settlor or beneficiaries. Trusts which are terminable at the will of the sole beneficiary are certainly valid, as in the case of a trust whereby a nominee holds immovable property for a beneficiary (eg *Strydom v De Lange* 1970 (2) SA 6 (T)). In trusts of this sort the nominee may well be bound to obey the instructions of the beneficiary as to the management of the property. Yet they are true trusts subject to the control of the court in regard to appointment and supervision (*Administrator Estate Cachalia v Dabhel Madressa Trust* 1940 WLD 14, *Ex Parte Thulsie* 1943 WLD 231, *Ex Parte Rajoo Dehal* 1937 WLD 136). Such a trust is distinguishable from mere agency by virtue of the fact that the trustee is *dominus* of the trust property and that the intention of the parties is to create a trust."

109 E Cameron "Constructive trusts in South African law: the legacy refused" (1999) 3 *Edinburgh LR* 342 353. The reference to Honoré is to the fourth edition of his book: T Honoré & E Cameron *Honoré's South African Law of Trust* 4 ed (1992).

that the arrangement fails the test of the establishment proposition and no trust will be established.

The above proposition is arguably uncontroversial. What is, however, altogether more opaque, is the question of what type and measure of control the parties must intend to bestow upon a trustee to meet the requirements of the establishment proposition.

This question is considered below.

4 5 Type of control relevant to the establishment proposition

The difference in perspective between the control test and the establishment proposition highlighted above is significant.[110] It accounts for why considerations of structural control may be relevant in determining the effective controller under the control test, but not for determining whether a trust has been established in accordance with the establishment proposition.

An investigation of what measure of structural control is afforded to third parties (apart from the trustees) fits snugly with the theoretical justification for the control test. In the context of holding the true controllers of a trust liable for the irresponsible exercise of such control, Flannigan has argued that sufficient structural control should attract principal status to controllers depending on what has been termed their "*in terrorem*" quality.[111]

This "*in terrorem*" quality refers to the persuasive power of structural control granted to others. Flannigan proposes that, where structural control over a trust is vested in persons other than the trustees, such controllers may abuse the threat of exercising this control to influence the manner in which the trustees exercise their asset control over the trust assets. The effectiveness of these threats is, according to him, directly proportional to the *in terrorem* quality of the structural control afforded to such third party; in other words, in the inherent quality of the structural right to strike fear or favour in the minds of the assets controllers – the trustees.

For example, where a founder has been vested with the structural right to dismiss and appoint trustees at will, it is conceivable that such a founder would be able to impose his will over the trustees in office, lest they run the risk of being removed.

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110 See part 4 4 1 above.

111 Flannigan (1986) *Est & Tr Q* 97 113.

The same holds for where a beneficiary is vested with the right to amend the trust provisions relating to trustee remuneration. These structural rights accordingly have a high *in terrorem* quality as they have the potential to influence the decisions by the trustees, either through explicit threat of use or through self-censorship of the trustees.

However, where structural control is limited to appointing replacement trustees upon a vacancy arising, such a right has little potential of influencing decisions of the trustees in office as it has no bearing upon them. Accordingly, such structural powers would have a low *in terrorem* quality.

Structural powers could, therefore, be sufficient to cause trustees to do what a beneficiary or founder "suggests" or "advises". The holder of the structural control may thus employ it to gain "effective asset control congruent with the scope of the function performed by the ostensible asset controller who is responsive to the *in terrorem* use of the right".[112]

I accept that the *in terrorem* quality of structural rights could result in trustees compromising their independence in favour of the holders of these rights. Therefore, the determination of the identity of structural controllers, and the measure of control that they enjoy, may be an important consideration in the context of Flannigan's control test. However, structural control (and its *in terrorem* quality) is not relevant in the context of the establishment proposition where the enquiry is limited to whether a valid trust has been established. This is so for two reasons.

The first is that the establishment proposition is only concerned with the status of the trust at its *establishment* and whether the trustees have the *capacity* to exercise independent judgement at that moment in time.[113] This postulates an objective examination based on the provisions of the trust deed.[114] An underlying assumption of importing structural control into the control test is that trustees may be swayed by the *in terrorem* quality thereof *in future*. This examination requires consideration that

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[112] 113-114.

[113] Over six decades ago, Caney J observed in *Moosa v Jhavery* 1958 4 SA 165 (N) at 169D-F:

"In my opinion the trust speaks from the time of its execution and must be interpreted as at that time. It is the settlor's intention at that time that must be ascertained from the language he used in the circumstances then existing. Subsequent events (and in these are included statutes) cannot, I consider, be used to alter that intention."

[114] See the text below n 78 in Chapter 3.

goes beyond the moment that the trust is established and requires one to consider the probable conduct of the trustees when faced with the threat of the exercise of structural control.

From this perspective, the investigation goes beyond the moment of the establishment of the trust and requires a subjective investigation regarding the likelihood of whether structural controllers would threaten the position of the trustees as well as the likelihood of the trustees succumbing to such threats.

The second reason relates to the second leg of the independence duality. Where the trustees hold effective asset control, structural controllers could only influence the manner in which the assets are managed where these trustees fail to act independently. This failure, it is submitted, constitutes a breach of the trustees' fiduciary duty and the consequences of such a breach, therefore, stand to be determined with reference to the fiduciary proposition.[115]

Asset control, on the other hand, is highly relevant in the context of the establishment proposition. As this type of control relates to the power to determine, directly, the manner in which the trust assets are to be employed, it strikes at the very core of the trust idea.

However, it is not inconceivable that structural control may also amount to effective asset control. In instances where structural control empowers a third party to assert direct asset control, and not rely on the *in terrorem* quality of the structural control, the structural control in question will also qualify as asset control. For example, where a founder retains the power to effect unilateral amendments to the trust deed, which include the manner in which the assets are to be employed, such structural control will be relevant for the purposes of the establishment proposition. The relevance however stems from the capacity of the founder to effect asset control through the exercise of structural control.

It follows that for purposes of the establishment proposition, the only determinative type of control is asset control. The question which follows is what measure of asset control is required to be held by trustees for a trust to be established.

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[115] See part 3 4 2 in Chapter 3.

4 6 Measure of asset control required

The varied application of the control test in the USA has caused one commentator to state that:

> "it is exceedingly difficult to make any accurate statement as to what powers may be given to the shareholders without subjecting them to personal liability".[116]

This difficulty is as present as ever in the context of the establishment proposition, and in particular regarding the measure of asset control required to establish a trust. However, an answer may be ventured when the emphasis placed on trusteeship as an office in South Africa is borne in mind.

It is uncontroversial to state that, at the very least, a trustee must be *dominus* of the trust property in the sense that he must be the proper functionary with the power to alienate, invest, distribute, or otherwise encumber the trust property. To hold otherwise, would conflict with the definition of a trust discussed in Chapter 3.[117]

What remains unclear is whether a trustee's discretion to exercise this facet of asset control may be restricted.

Conventional wisdom suggests that it may. The South African legal landscape is strewn with trusts where the trustees are afforded varying levels of discretion in the administration of the trust estate, from being granted absolute discretion to no room for discretion at all.

It is tempting, therefore, to propose a minimum test of discretion that is required for the validity of a trust. However, consider an arrangement where a founder transfers assets to a trustee for the sole purpose of investing same in a nominated account until a specified date, whereafter the trustee is directed to pay same to a beneficiary. In these circumstances, the trustee has no discernible discretion in the employment of the trust assets, but the arrangement is clearly still a trust.

On the other hand, an arrangement where assets are made over to a trustee, who must administer it according to the absolute direction of the founder or others, sits uncomfortably with the definition of trust discussed in Chapter 3 because such a trustee has no control over the trust assets.

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116 GG Bogert *The Law of Trusts and Trustees* 2 ed (1964) para 297.

117 See the text to n 90 in Chapter 3.

What, then, is the distinction between these two scenarios? In my view, the answer lies in the legal construction of trusteeship as an office. The appreciation of trusteeship as a *quasi*-public office allows for an interpretation where full asset control (including absolute discretionary power) is vested in that office, with the *exercise* of such discretion being regulated by the trust deed.

Once it is appreciated that the full complement of asset control vests in the office of trusteeship, but that the employment of that control is subject to the trust deed (and not the whim of another) the distinction between the two scenarios highlighted above appears clearly.

Irrespective of whether a trust deed limits the exercise of a trustee's discretion, same is still vested in that office and not in the hands of the founder or third parties. This construction accounts for why an amendment of the trust may permit for a variation of a trustee's discretion. Such an amendment does not transfer discretion from one functionary to another; it merely amends the basis upon which it is exercised.

This construction also accounts for why no trust is established where the founder does not divest himself of all control in favour of the office of trusteeship.

It is accordingly proposed that the measure of asset control that is to be afforded to trustees is absolute, but there can be no objection to the exercise of this control being restricted through the trust deed from time to time as all asset control remains vested in the office of trusteeship.

4 7 Conclusion

In this chapter, the establishment proposition is examined with reference to the control test developed in the USA. It is argued that there are key distinctions between the control test and the establishment proposition.

Key among these distinctions is that the focus of the control test is to unmask the true controllers of the trust, whereas the focus of the establishment proposition is to determine whether the trustees are afforded sufficient control for the arrangement to comply with the core idea of the trust.

This distinction results therein that the control test is often subjective and also takes into account the probable effects of structural control on the future conduct of

the trustees, whereas the establishment proposition is objective and limited to the moment of the establishment of the trust.

Consequently, the establishment proposition is not concerned with the identity of structural controllers but with whether the trustees are afforded a sufficient measure of asset control. It is proposed that absolute asset control is to be afforded to the office of trusteeship in order to meet the requirements of the establishment proposition.

The limitation that may be placed on the discretionary asset control may be explained on the basis that full discretionary control is still vested in the office of trusteeship, but that key decisions in respect thereto are grounded in the trust deed that informs the office.

As appears from the discussion in Chapter 6, the establishment proposition as developed in this chapter plays an important role in considerations relating to so-called “sham trusts”.

In the following chapter, Chapter 5, the fiduciary proposition is examined in further detail. This proposition is relevant in the manner in which the administration of the trust is evaluated and applies only once a trust is established. This proposition as a part of the independence duality model plays an important role to explain the consequences of a failure of a trustee to administer the trust estate independently once afforded the capacity to do so.

Accordingly, consideration of the principles of the fiduciary proposition only arises once it is clear that the requirements of the establishment proposition have been satisfied.

CHAPTER 5: THE FIDUCIARY PROPOSITION

5 1 Introduction

It is now settled that a trustee has a duty to bring an independent mind to bear upon the administration of the trust.[1] However, this duty may be skirted in a number of ways. Examples include: not participating in the administration of the trust; acting as what has been referred to as a "sleeping trustee";[2] or through habitual deference to a dominant trustee, the founder, beneficiaries, or other third parties.[3]

Notwithstanding the general consensus that there is no place for such a form of trusteeship in South African law,[4] a review of relevant case law and academic commentary suggests that the exact basis, or theoretical underpinnings, of a trustee's duty of independence, has not yet been settled.[5]

One explanation is that the duty of independence flows from the requirement of trustees to act jointly in the administration of the trust, which in turn is required as a result of the so-called "joint-action rule".[6]

In this chapter, the above proposition is critically examined with a particular focus on the underpinnings of the joint-action rule. The conclusion is reached that this rule does not adequately explain a trustee's duty of independence because it is not applicable to the internal administration of the trust. This is not to say that trustees are not compelled to act collectively in the administration of the trust, but, as is elucidated below, it is submitted that this requirement is as a result of the joint occupation of the office of trusteeship.

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1 F du Toit "The fiduciary office of trustee and the protection of contingent trust beneficiaries" (2007) 18 *Stell LR* 469 475.

2 MJ de Waal "The liability of co-trustees for breach of trust" (1999) 10 *Stell LR* 32.

3 *Tjimstra NO v Blunt-MacKenzie NO* 2002 1 SA 459 (T). See also, *Jordaan v Jordaan* 2001 3 SA 288 (C); *Badenhorst v Badenhorst* 2006 2 SA 255 (SCA); *Stander v Schwulst* 2008 1 SA 81 (C); *Wiid v Wiid* NCHC 13-01-2012 case no 1571/2012.

4 L Olivier "Trusts: traps and pitfalls" (2001) 118 *SALJ* 224 229-230; *Tjimstra NO v Blunt-MacKenzie NO* 2002 1 SA 459 (T) 474E-F.

5 See also, *Smit v Van der Werke* 1984 1 SA 164 (T); *Goolam Ally Family Trust t/a Textile, Curtaining and Trimming v Textile, Curtaining and Trimming (Pty) Ltd* 1989 4 SA 985 (C); *Coetzee v Peet Smith Trust* 2003 5 SA 674 (T); *Steyn NO v Blockpave (Pty) Ltd* 2011 3 SA 528 (FB); F du Toit "A trustee's duty of independence" (2009) 73 *THRHR* 637; F du Toit "Co-trusteeship and the joint-action rule in South African trust law" (2013) 27 *Trust Law International* 18.

6 Du Toit (2009) *THRHR* 637.

Against this background, it is argued that the fiduciary proposition,[7] within the context of the dual independence dichotomy highlighted in Chapter 3, provides the theoretical framework within which a trustee's duty to bring an independent mind to bear upon the administration of the trust is to be explained and evaluated.

To conduct this analysis, a brief review of the manner in which a fiduciary relationship arises is required. Accordingly, this chapter commences with a discussion of the nature and ambit of fiduciary relationships in general, and the tests developed to evaluate whether a specific relationship gives rise to a fiduciary duty.

This analysis is then applied in the context of trusts, which leads to the evaluation of the joint-action rule as justification for trustee independence, compared to that of the fiduciary proposition.

5 2 How is a fiduciary duty established?

The term "fiduciary duty" has proven surprisingly difficult to define with sufficient clarity and has been described as "a legal obligation in search of a principle".[8]

What is clear, is that fiduciary duties exist in the context of particular relationships[9] and that certain relationships have been clearly accepted as being fiduciary in nature. Examples of accepted fiduciary relationships include the relationship between an agent and principal, employee and employer, directors and companies, partners, and trustees and beneficiaries.[10] However, the list of fiduciary relationships is not a closed one.

The Canadian experience is helpful in considering whether a measure may be developed for the recognition of a fiduciary relationship. Between 1984 and 1994, the Supreme Court of Canada (the "SCC") considered and enforced fiduciary duties in varying contexts and developed what has been referred to as the "fiduciary principle".

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7 See part 3 3 2 in Chapter 3. See also, PA Olivier *Trustreg en Praktyk* (1989) 37; Du Toit (2009) *THRHR* 637; PA Olivier, S Strydom & GPJ van den Berg *Trust Law and Practice* (SI 6 2018) 2-15.

8 *Hodgkinson v Simms* 1994 3 SCR 377 415. See also, K Idensohn "Towards a theoretical framework of fiduciary principles: *Volvo (South Africa) (Pty) Ltd v Yssel* 2009 4 All SA 497 (SCA)" (2010) 2 *Speculum Iuris* 142; Du Toit (2007) *Stell LR* 3; E Nel "Unfettered, but not unbridled: the fiduciary duty of the trustee" (2016) 37 *Obiter* 436.

9 *Robinson v Randfontein Estates Gold Mining Co Ltd* 1921 AD 168 177.

10 Idensohn (2010) *Speculum Iuris* 142.

The first of these cases was *Guerin v The Queen* ("*Guerin*"),[11] a landmark decision on Aboriginal rights, in which the SCC held that the government owed a fiduciary duty to the indigenous people of Canada and confirmed *Aboriginal title* as a common-law doctrine.[12]

In confirming that fiduciary duties transcend accepted relationships, Dickson J, writing for the majority of the court, held as follows:

> "It is sometimes said that the nature of fiduciary relationships is both established and exhausted by the standard categories of agent, trustee, partner, director and the like. I do not agree. It is the *nature* of the relationship, not the specific category of actor involved that gives rise to the fiduciary duty. The categories of fiduciary, like those of negligence, should not be considered closed."[13]

In *Frame v Smith* ("*Frame*")[14] Wilson J, in a dissenting judgment, expounded upon the conceptual approach to fiduciary relationships in *Guerin*, and proposed a three-step analysis to guide the court in identifying new fiduciary relationships.[15] She proposed that fiduciary relationships are marked with the following three characteristics:

(i) scope for the exercise of some discretionary power;
(ii) that power or discretion can be used unilaterally so as to effect the beneficiary's legal or practical interests; and
(iii) a peculiar vulnerability to the exercise of that discretion or power.[16]

In *Hodgkinson v Simms* ("*Hodgkinson*"),[17] a matter where a stockbroker sought to hold his accountant liable for losses incurred in investing in a real estate project, the

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11 1984 2 SCR 335.

12 Aboriginal title refers to the doctrine that land rights of indigenous people survive the assumption of sovereignty under colonialism: See, Duhaime's *Law Dictionary* <http://www.duhaime.org/LegalDictionary/A/AboriginalTitle.aspx> (accessed 08-09-2018). For an in-depth discussion of Aboriginal title, see AJ Ray *Aboriginal Rights Claims and the Making and Remaking of History* (2016) 68.

13 384 (emphasis added).

14 1987 2 SCR 99.

15 The SCA in *Phillips v Fieldstone Africa (Pty) Ltd* 2004 3 SA 465 (SCA) 482C endorsed these steps as helpful, but not determinative.

16 136.

SCC cautioned against employing the three-step test set out in *Frame*.[18] It did so on the basis that it does not apply in circumstances where fiduciary duties, though not innate to a given relationship, arise from the particular circumstances of that specific relationship.

In determining whether a fiduciary relationship existed, the court held that:

> "the question to ask is whether, given all the surrounding circumstances, one party could reasonably have expected that the other party would act in the former's best interests with respect to the subject matter at issue. Discretion, influence, vulnerability and trust are non-exhaustive examples of evidential factors to be considered in making this determination."[19]

and

> "In summary, the precise legal or equitable duties the law will enforce in any given relationship are tailored to the legal and practical incidents of a particular relationship. To repeat a phrase used by Lord Scarman, '[t]here is no substitute in this branch of the law for a meticulous examination of the facts'".[20]

The Canadian authorities, therefore, underscore that it is the nature of the relationship, and not the conduct of the parties, that is determinative of the existence of a fiduciary duty.[21] That this also applies in South Africa, appears from the differing outcomes of two early cases that bear a factual resemblance, but are nevertheless distinguishable.

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17 1994 3 SCR 377

18 1987 2 SCR 99.

19 417.

20 421, quoting from *National Westminster Bank plc v Morgan* 1985 1 All ER 821 (HL) 831.

21 This sentiment, that it is undesirable to lay down a general test for the recognition of a fiduciary relationship, is echoed by Gibbs CJ of the High Court of Australia in *Hospital Products Ltd v United States Surgical Corporation* 1984 156 CLR 41 (HC of A) 69 as follows:

"I doubt if it is fruitful to attempt to make a general statement of the circumstances in which a fiduciary relationship will be found to exist. Fiduciary relations are of different types, carrying different duties and a test which might seem appropriate to determine whether a fiduciary relationship existed for one purpose might be quite inappropriate for another purpose."

The first is *Burland v Earle* ("*Burland*"),[22] a decision of the Privy Council on appeal from the Court of Appeal for Ontario, and the second *Robinson v Randfontein Estates Gold Mining Co Ltd* ("*Robinson*"),[23] a decision of the Appellate Division (as it then was) on appeal from the Transvaal Provincial Division of the High Court.

Burland concerned the conduct of a member of a joint-stock company, the British American Bank Note Company ("the Bank Note Company"). The Bank Note Company conducted business in the engraving and printing of banknotes, debentures, stamps, and other bills of exchange. This business proved highly successful courtesy of printing contracts with various governments and regular, generous, dividends were paid to its shareholders.

Burland was the majority shareholder and the president of the company and Earle its second-largest shareholder. Shortly before the commencement of litigation, the company lost a lucrative contract with the Dominican Republic, causing its profits to decline significantly. On 7 December 1897, Earle, together with other shareholders, commenced action against Burland claiming, *inter alia*, repayment of profits he made by selling property to the Bank Note Company while he was president thereof.[24]

In addition to his association with the Bank Note Company, Burland was also a shareholder and creditor of a company situated in Montreal, the Burland Lithographic Company. This company, having become insolvent, was wound-up and Burland purchased from the liquidator certain lithographic plant equipment for a sum of $21 564, which he subsequently on-sold to the Bank Note Company for $60 000. The evidence suggested that Earle and the other shareholders were aware of the sum for which Burland purchased the equipment and that the price paid by the Bank Note Company was market-related.

The trial court ordered Burland to pay to the Bank Note Company the sum of $38 436, being the amount of the profit realised by him on the resale, which order the Ontario Court of Appeal affirmed.

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22 1902 AC 83.

23 1921 AD 168.

24 All in all, the plaintiffs prosecuted four claims against Burland and, initially, the company, relating to (i) payment of a reserve fund to shareholders as dividends; (ii) a claim regarding the manner in which this fund was invested; (iii) payment by Burland of profits realised in the on-sale of goods to the company; and (iv) allegations of an improper salary drawn by Burland. For present purposes, only the payment of profits by Burland is relevant.

However, on appeal to the Privy Council, these orders were set aside and it was held that Burland was entitled to retain the profits from the resale of the lithographic plant equipment. Lord Davy, delivering the judgment, stated as follows:

> "There is no evidence whatever of *any commission or mandate to Burland to purchase on behalf of the company or that he was in any sense a trustee for the company of the purchased property*. It may be that he had an intention in his own mind to resell it to the company, but it was an intention which he was at liberty to carry out or abandon at his own will. It may be also that a person of a more refined self-respect and a more generous regard for the company of which he was president would have been disposed to give the company the benefit of his purchase. But their Lordships have not to decide questions of that character. The sole question is whether he was under any legal obligation to do so. Let it be assumed that the company or the dissentient shareholders might by appropriate proceedings have at one time obtained a decree for rescission of the contract. But that is not the relief which they ask or could in the circumstances obtain in this suit."[25]

From the above, it is clear that the result may have been different if Burland stood in a relationship of agency or other facts were present upon which he was deemed to be a trustee of the company. However, in the circumstances, the Privy Council held that the relationship between the parties was such that Burland was at liberty to transact in his own interest and the relief claimed by the Bank Note Company was refused.

In contrast, the South African Appellate Division in *Robinson*[26] upheld a claim by the respondent company (the plaintiff in the court *a quo*) against a former director and shareholder for profits made in the on-sale to it of certain farmland and mining rights. Innes CJ, writing for the majority of the Appellate Division, referenced *Burland*[27] with approval and emphasised that it is the nature of the relationship between parties that is determinative of whether a fiduciary duty is owed.

The court pointed out that the existence of a relationship of agency was a powerful pointer to such a fiduciary relationship, but emphasised that it is by no means the only consideration:

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25 99 (emphasis added).

26 1921 AD 168.

27 1902 AC 83, referenced in the judgment as "*Borland v Earle* 1902 AC 83".

> "Whether a fiduciary relationship is established will depend upon the circumstances of each case. Where the director was at the date of the acquisition the agent of the company for such transaction, the fiduciary relationship would of course be created. That element has generally been present in the decided cases where profits have been awarded. But, so far as I am aware, it is nowhere laid down that in these transactions there can be no fiduciary relationship to let in the remedy without agency. And it seems hardly possible on principle to confine the relationship to agency cases. There may surely be circumstances, apart from mandate, where a duty to acquire for the company may be inferred."[28]

As if to further emphasise that the nature of the relationship between parties was determinative of the issue, the court referred to the result in *Burland* and drew a distinction with that case as follows:

> "An order to account for profits was refused in *Borland v Earle*, not merely because there was no mandate to purchase for the company, but because there was neither such a mandate, nor *other circumstances* which would have made the director a trustee of the company."[29]

As testament to its adequacy and reflection of the importance of the principles highlighted therein, the SCA again endorsed the above passages in *Robinson*,[30] in *Phillips v Fieldstone Africa (Pty) Ltd* ("*Phillips*")[31] together with the position elucidated in *Hodgkinson*[32] discussed above.

The *Phillips* matter concerned the liability of an employee to account to his employer for secret profits made out of an opportunity that arose in the course of his employment.[33] At issue was whether the employee had a fiduciary duty to the employer to declare the secret profit. Counsel for the appellant (the employee) emphasised that the particulars of claim contained no reference in terms of a fiduciary duty. The submission was accordingly that the respondent was unable to rely on the existence of a fiduciary duty between the parties. The court, per Heher

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28 180.

29 180 (emphasis added).

30 1921 AD 168.

31 2004 3 SA 465 (SCA).

32 1994 3 SCR 377.

33 2004 3 SA 465 (SCA) para 1.

JA, famously held that "There is no magic in the term 'fiduciary duty'".[34] The court proceeded to explain:

> "The existence of such a duty and its nature and extent are questions of fact to be adduced from a thorough consideration of the substance of the relationship and any relevant circumstances which affect the operation of that relationship… While agency is not a necessary element of the existence of a fiduciary relationship… that agency exists will almost always provide an indication of such a relationship. The emphasis in the particulars of claim upon the representative nature of the appellant's status in dealing with Safika [the counterparty in the transaction with the respondent] and the duty to account for profits acquired by him in that capacity should have been to counsel an unmistakable beacon which marked the claim as one in which the appellant stood toward the respondents in a position of confidence and good faith which he was obliged to protect."[35]

The defence that the fiduciary relationship was not pleaded accordingly failed as the pleading of the nature of the relationship between the parties was regarded as sufficient notice of the existence of a fiduciary relationship.

The significance of the nature of the relationship between the parties as an indication of the existence of a fiduciary duty was again emphasised by the SCA in the matter of *Volvo (South Africa) (Pty) Ltd v Yssel* ("*Volvo*").[36] That matter now provides further insight into the South African approach to the question of determining both the existence, and ambit, of a fiduciary duty.

The facts of the case were as follows. After commencing operations in 2000, Volvo (South Africa) (Pty) Ltd ("Volvo"), the appellant in the SCA, required the services of a manager for its information technology ("IT") division. A third-party recruitment agency introduced Mr Yssel ("Yssel"), the respondent, to Volvo, who decided to appoint him to the position.[37]

Yssel did not favour entering into direct employment with Volvo and on his insistence, he was instead employed indirectly through the services of a labour broker, Highveld Personnel (Pty) Ltd ("Highveld").[38] For the next five years, Yssel's

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34 Para 27.

35 Para 27.

36 2009 6 SA 531 (SCA).

37 Para 1.

38 This arrangement was presumably due to tax considerations: see Idensohn (2010) *Speculum Iuris* 143.

services were rendered to Volvo through Highveld, who would invoice Volvo and in turn pay Yssel. In making these arrangements, Volvo had no direct contact with Highveld and all dealings were solely done through Yssel.[39]

By 2004, the IT department of Volvo had expanded to include six more persons who were similarly employed by labour brokers (other than Highveld) and who assigned their services to Volvo ("the personnel"). By middle 2004, Yssel approached the human resources manager of Volvo, Ms Van Eeden, and told her that some of the personnel were unhappy with their respective labour brokers and that he could arrange for them to be transferred to Highveld at no extra cost to Volvo. Yssel also suggested to the other personnel that their remuneration could be more favourably structured if they render their services to Volvo through Highveld.[40]

On the basis of these proposals, a master agreement was concluded between Volvo and Highveld in terms of which it was agreed that Highveld would supply the services of the personnel to Volvo in return for a monthly fee that was to be stipulated in each case in an annexure to the master agreement. Subsequently, and over a period of time between August 2004 and April 2005, Yssel accompanied each of the six other personnel members to the offices of Highveld where they were introduced to an officer of Highveld, Ms Pieterse ("Pieterse"), and signed the annexures to the master agreement. All the personnel testified that they were led to understand that from the fees Highveld charged to Volvo, Highveld would retain a fixed charge of R425 per month and an administration fee of 3% on their earnings. None of the personnel were, however, aware of the rate at which their services were being charged to Volvo.[41] Upon the conclusion of each annexure, Highveld proceeded to invoice Volvo for the services of the relevant personnel.

Significantly, Volvo had no direct contact with Highveld in these dealings and at all times dealt only through Yssel. Unbeknown to Volvo, or the personnel concerned, Yssel had arranged with Pieterse that a portion of the payment made by Volvo would be paid to him as a "commission" for arranging the transfer of the personnel to Highveld. Yssel and Pieterse also conspired to keep the payment of the commission

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39 Para 2.

40 Para 4.

41 Para 5.

secret from both Volvo and the personnel.[42] The payments received by Yssel in this respect were significant and represented approximately 40% of all payments made by Volvo to Highveld.[43]

The truth was exposed when at the end of 2005 one of the personnel, Steyn, came across a document reflecting the payment Volvo made to Highveld in respect of his services. This evidenced a clear shortfall in what he, in turn, was paid by Highveld. At first, Steyn turned to Yssel for an explanation, but when no satisfactory explanation was forthcoming, he pressed on and discovered other, similar documents, whereupon the matter was escalated to the senior personnel of Volvo.[44]

The matter came to the attention of Van Eeden in January 2006, who subsequently arranged for a meeting with Pieterse. This was the first time that any representative of Volvo, other than Yssel, had any dealings with an officer of Highveld. When confronted with the discrepancies between that paid to Highveld by Volvo and that paid over to the relevant personnel, Pieterse at first denied any payment to Yssel, but later relented and admitted to the commission scheme involving Yssel. When Yssel learnt of the meeting later that day, and while Van Eeden was in the process of preparing a letter suspending him, he delivered a letter of resignation. The remaining personnel immediately terminated their relationship with Highveld and accepted direct employment with Volvo.[45]

Subsequent investigations by Volvo's internal auditor revealed that between August 2004 and January 2006, Volvo paid a sum of R1 967 900 to Highveld in respect of the services rendered by the personnel concerned (excluding Yssel). Of this sum, only R1 087 650 was paid over to the personnel, with Highveld retaining R114 143 and the balance of R775 107 paid to Yssel.

Based on this discovery, Volvo instituted action against Yssel in the Witwatersrand Local Division,[46] claiming repayment of the R775 107 paid to Yssel by Highveld on the basis that it was secret profits made through a breach of fiduciary

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42 Para 7.

43 Para 7. As per example, Volvo paid the sum R27 400 to Highveld in respect of the services of one of the personnel in January 2006. Of this sum, R12 000 was paid to the person concerned with the balance of R15 400 being paid to Yssel.

44 Para 9.

45 Para 10.

46 The judgment *a quo* is reported as *Volvo SA (Pty) Ltd v Yssel* 2008 3 All SA 488 (W).

duty.[47] It was argued on behalf of Yssel that, in view of the successive written agreements between Volvo and Highveld, and the lack of privy of contract between him and Volvo, he did not owe Volvo a fiduciary duty.[48]

In the alternative, it was submitted that in as far as any fiduciary relationship may have existed between him and Volvo, Yssel did not breach the nature and duties attaching thereto.

In order to determine liability, the court was therefore called upon to decide, first, whether Yssel owed Volvo a fiduciary duty, and if so, the nature and extent of this duty.

After referencing *Burland*[49] and *Robinson*,[50] the court *a quo* held that, given the nature and scope of Yssel's responsibilities, a fiduciary relationship did exist between him and Volvo,[51] but that Yssel's duties in this respect were limited to the management of Volvo's IT department and did not extend to the recruitment of the personnel.[52] Accordingly the court *a quo* refused Volvo's claim.

On appeal, the SCA endorsed the sentiment in *Hodgkinson*[53] that the existence of a fiduciary relationship must be determined by the nature of the relationship between the parties, but cautioned against an interpretation of that case that suggests some "mutual understanding" between the parties as a pre-requisite for a fiduciary relationship.

Instead, the court held that "[w]hat is called for is an assessment, upon a consideration of all the facts, of whether reliance by one party upon the other was justified in the circumstances".[54]

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47 The claim for secret profits made through breach of a fiduciary duty is a *sui generis* claim and is not based on contract or delict. Accordingly, it is not a claim for damages and the fact whether the claimant suffered any damage is of no consequence – *Volvo SA (Pty) Ltd v Yssel* 2008 3 All SA 488 (W) para 54. See also, *Robinson v Randfontein Estates Gold Mining Co Ltd* 1921 AD 168 and *Phillips v Fieldstone Africa* (Pty) Ltd 2004 3 SA 465 (SCA).

48 *Volvo SA (Pty) Ltd v Yssel* 2008 3 All SA 488 (W) para 63.

49 1902 AC 83.

50 1921 AD 168.

51 *Volvo SA (Pty) Ltd v Yssel* 2008 3 All SA 488 (W) paras 68-71.

52 Para 72.

53 [1994] 3 SCR 377 (SCC) ((1995) 117 DLR (4th) 161).

54 2009 6 SA 531 (SCA) para 17.

On this basis the SCA held that a fiduciary relationship had arisen between Volvo and Yssel and expressed itself as follows:

> "Yssel was well aware that Van Eeden had made no independent enquiries relating to the arrangement with Highveld and was acting entirely upon what she was told by him. That he found it necessary to secure an agreement of secrecy from Pieterse makes it abundantly clear that he was well aware that Van Eeden believed that he was arranging matters pursuant to his ordinary managerial duties and not for his own account. In short, he was well aware that Van Eeden did not consider herself to be dealing at arm's length with an independent broker who was arranging matters on his own account, but was dealing with the manager of the division concerned. It was only because Yssel was the manager that the transaction came about at all. I have no doubt that Yssel was in a position of trust when he engaged himself in the matter and was not entitled to allow his own interests to prevail over those of Volvo. He is obliged in those circumstances to disgorge his secret commissions and the appeal must succeed."[55]

This matter illustrates that the particular relationship between the parties does not only determine the existence of a fiduciary relationship, but also its nature and extent. The position adopted in *Volvo* was approved and applied in the matter of *Attorneys Fidelity Fund Board of Control v Intibane Mediates* ("*Intibane*").[56]

In that matter, the Attorneys Fidelity Fund ("the AFF") mandated Mr Ramathibe (who traded as the first defendant) to identify a suitable immovable property to serve as their headquarters. Ramathibe discharged his mandate by identifying a property owned by two companies, Erf 49-1 (Pty) Ltd and Head Brothers (Pty) Ltd, the third and fourth defendants in the action ("the sellers").[57] In their dealings with the AFF, the sellers were represented by Mr Roome. Ultimately, the property concerned was purchased for a sum of R37.5 million, which sum Roome presented as the sellers' "bottom line".[58]

However, before the transfer of the property to the AFF could be completed, it came to light that Roome had a separate, and secret, agreement with Ramathibe to the effect that the latter could retain the balance of any sale in excess of R32 million as a commission that was not to be disclosed to the AFF.[59] Details of this agreement

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55 Para 20.

56 2016 6 SA 415 (GP).

57 Para 2.

58 Para 6.

59 Para 43-46.

were contained in non-disclosure agreements between Roome and Ramathibe in order for it to be kept from the AFF. Transfer of the property was nevertheless proceeded with and the R5.5 million rand commission (representing the excess of the purchase over R32 million) was retained in the transferring attorney's trust account, pending the finalisation of the proceedings for recovery initiated by the AFF.[60] The central issue for consideration was whether Roome was under a legal duty to have disclosed his agreement of a secret commission with Ramathibe to the AFF.[61]

In holding that there was such a duty on Roome, Potterill J endorsed the principle enunciated in *Volvo* that "[w]hat is called for is an assessment, upon a consideration of all the facts, of whether reliance by one party upon the other was justified in the circumstances":[62]

> "There is in my mind no doubt that Roome can in law never be entitled to the commission he agreed to with Ramothibe and should be disgorged thereof. Roome had a relationship with the AFF's agent, Ramothibe. He also had a relationship with the AFF directly; he emailed it and met with representatives of the AFF. He knew that Ramothibe was acting on behalf of the AFF in obtaining the premises. He knew that as incentive for Ramothibe to promote his properties, he (Roome) was agreeing to commission in non-disclosure and confidentiality agreements to which the AFF was not privy. In assessing all these facts the question to be answered is whether it was justified for the AFF to rely on the conduct of Roome."[63]

In view of the prevailing circumstances, Potterill J held that the AFF could reasonably have expected Roome to inform it that Ramathibe, who was appointed as its agent, was conspiring against its interest by negotiating an inflated purchase price.[64] In the circumstances, by representing that the sellers' "bottom line" was R37,5 million when, in reality it was R32 million, Roome made a wrongful misrepresentation on account of which the defendants were held liable to the AFF for damages in the sum of R5.5 million.[65]

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60 Para 3.

61 Para 109.

62 2009 6 SA 531 (SCA) para 17.

63 Para 105.

64 Para 106.

65 Para 114.

These two cases illustrate that there is no one-size-fits-all approach in determining the existence and nature of a fiduciary duty. What is called for is an assessment, upon consideration of all the available facts, of whether reliance by one party upon the other was justified.[66] It follows, therefore, that a fiduciary duty arises where parties stand in a position of trust towards each other and the extent of this duty is determined by the relationship between the parties.[67]

5 3 Fiduciary duties grounded in the office of trusteeship

In view of the fluidity of a fiduciary relationship, and the difficulty in developing a single test for its existence, it is unsurprising that the nature of a trustee's fiduciary duty has proven difficult to define.

Du Toit[68] points out how South African courts have intermittently referred to a trustee's "fiduciary duty" (in the singular),[69] and a trustee's "fiduciary duties" (in the plural)[70] and how divergent views exist as to the trustee's counterpart in the fiduciary relationship ranging between the trust property,[71] on the one hand, and the beneficiaries, on the other.[72]

In an instructive contribution, Du Toit has unpacked the fiduciary duty of a trustee in the narrow sense.[73] He has shown how a trustee's fiduciary duty stems from the *office* of trusteeship and that the trustees all occupy one, unitary, composite office.[74] In particular, Du Toit has shown how section 9(1) of the TPCA now reflects the

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66 *Volvo (Southern Africa) (Pty) Ltd v Yssel* 2009 6 SA 531 (SCA) 537A.

67 See also the instructive discussion of the *Volvo* case by Idensohn (2010) *Speculum Iuris* 142.

68 Du Toit (2007) *Stell LR* 472.

69 *Hofer v Kevitt* 1996 2 SA 402 (C) 407F.

70 *Doyle v Board of Executors* 1999 2 SA 805 (C) 813C-D; *Bafokeng Tribe v Impala Platinum Ltd* 1999 3 SA 517 (BHC) 546B. See in this regard, Du Toit (2007) *Stell LR* 469 472.

71 *Louw v Coetzee* 2003 3 SA 329 (SCA) 336A-B; *African Bank Ltd v Weiner* 2003 All SA 50 (C) 54D-E.

72 *Doyle v Board of Executors* 1999 2 SA 805 (C) 813B; *Jowell v Bramwell-Jones* 2000 3 SA 274 (SCA) 284C-D.

73 Du Toit (2007) *Stell LR* 469.

74 471. See also, MJ de Waal "Die wysiging van 'n *inter vivos* trust" (1998) *TSAR* 326 331; *Doyle v Board of Executors* 1999 2 SA 805 (C) 813A-B.

common-law standard in respect of trustees' trust administration[75] and that there is one, single, fiduciary duty. In this regard, Du Toit states that:

> "a South African trustee is under a single fiduciary duty, which can conveniently be called a 'general fiduciary duty' … [T]his general fiduciary duty is multi-faceted in that it is comprised of a number of specific component duties. Which component duty or duties of a trustee's general fiduciary duty will be relevant in any given instance will depend, as indicated by the court in the *Phillips* case, on the facts at hand adduced from the substance of the relationship between the relevant parties, as well as any relevant circumstances which affect the operation of such relationship."[76]

Du Toit's submissions in this respect are well motivated and must be supported. He proceeds to identify at least four specific component fiduciary duties, being the duty of care,[77] the duty of impartiality,[78] the duty of independence[79] and the duty of accountability.[80] For present purposes, it is the identification of the duty of independence that is most relevant. In this regard, Du Toit argues:

> "A third component of a trustee's general fiduciary duty is that he is duty bound to exhibit a minimum degree of independence in respect of trust administration – a trustee, as a fiduciary office-holder, should exercise independent judgment in respect of trust administration and should not merely slavishly follow the lead of the trust founder, his co-trustees or the trust beneficiaries. Cameron JA acknowledged a trustee's independence in *Land and Agricultural Development Bank of SA v Parker* as an essential of trusteeship, stemming from the 'core idea' of the trust, when he stated that the functional separation of a trustee's ownership (or control) over trust property from any benefit consequent thereupon 'tends to ensure independence of judgment on the part of the trustee – an indispensable requisite of office.'"[81]

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75 Section 9(1) of the TPCA provides that:
"[a] trustee shall in the performance of his duties and the exercise of his powers act with the care, diligence and skill which can reasonably be expected of a person who manages the affairs of another."

76 Du Toit (2007) *Stell LR* 473. The reference to the "*Phillips* case" is to *Phillips v Fieldstone Africa (Pty) Ltd* 2004 3 SA 465 (SCA).

77 473; *Metequity Ltd v NWN Properties Ltd* 1998 2 SA 554 (T) 556I-J.

78 Du Toit (2007) *Stell LR* 474; *Jowell v Bramwell-Jones* 2000 3 SA 274 (SCA).

79 Du Toit (2007) *Stell LR* 475; *Land and Agricultural Bank of South Africa v Parker* 2005 2 SA 77 (SCA).

80 Du Toit (2007) *Stell LR* 475; *Doyle v Board of Executors* 1999 2 SA 805 (C).

81 Du Toit (2007) *Stell LR* 475.

It is submitted that in the context of trusts, there are two sets of relationships that give rise to a trustee's fiduciary duty. First, a trustee is entrusted with certain assets by the founder of the trust who surrenders control thereof in favour of the trustee. This act of surrendering control is indicative of the relationship of reliance and trust that is specific to the particular trustee.

In addition, the relationship of trust between trustee and beneficiary, and in particular the separation of control from benefit,[82] underscores the fact that beneficiaries are required to place reliance upon the trustees for the responsible administration of the trust estate. It is therefore clear, in view of the position adopted in *Phillips*,[83] *Volvo*[84] and *Intibane*,[85] that the nature of the relationship between the parties is decisive, that the duty to bring an independent mind to bear upon the administration of the trust must form part of a trustee's fiduciary duty. In view of the functional separation between control and benefit over trust assets there can be no doubt that a mutual understanding between founder, trustee and beneficiary, that the trustee will play an active and independent role in the administration of the trust, exists.

The duty of independence as a facet of a trustee's fiduciary duty appears clearly from the matter of *Wiid v Wiid* ("*Wiid*"),[86] a decision of the Northern Cape High Court, Kimberley, in which trustees were held to account for their failure to bring an independent mind to bear upon the administration of the trust.[87]

The *Wiid* case related to a typical family trust, the Elwida Trust, in which the founder, a game farmer and the family patriarch (who was already deceased at the time of the hearing of the matter), settled a trust for the benefit of his wife, their children and other lawful descendants.[88] The trust was a discretionary trust in the sense that the trust deed provided that the trustees could:

> "in hulle uitsluitlike diskresie al die of enige van die Inkomstebegunstigdes ingevolge hierdie Trust, vrye gebruik en genot mag toelaat van enige bates waarvan die Trust die

82 *Land and Agricultural Bank of South Africa v Parker* 2005 2 SA 77 (SCA).

83 *Phillips v Fieldstone Africa (Pty) Ltd* 2004 3 SA 465 (SCA).

84 *Volvo (Southern Africa) (Pty) Ltd v Yssel* 2009 6 SA 531 (SCA).

85 *Attorneys Fidelity Fund Board of Control v Intibane Mediates* 2016 6 SA 415 (GP).

86 NCHC 13-01-2012 case no 1571/2012.

87 For an in-depth discussion of the *Wiid* case see Nel (2016) *Obiter* 436.

88 Para 2.3.

> eienaar is, en mag besluit of die Trust of die betrokke Inkomstebegunstigdes vir die instandhouding van die bates asook die betaling van enige belastings, versekeringspremies en ander soortgelyke koste verantwoordelik moet wees."[89]

The Elwida Trust was established during 1992 with the founder, his wife ("Mrs Wiid"), daughter ("Van Loggenberg") and a Mr Erasmus (a bookkeeper) as the trustees.[90] During or about December 1999, Erasmus resigned as trustee and a Mr Du Toit ("Du Toit") (also a bookkeeper) and the founder's son, Jacobus Philipus Wiid ("Jacobus"), were appointed as trustees.

The founder had operated all the family farming operations in the trust, which included holding various farms, game, and livestock therein.[91] During August 2001, the trustees of the Elwida Trust leased all the farms, game, and livestock they held to Jacobus on extremely generous terms. A nominal rental was charged for the lease of the farms and the livestock, and no rental was charged for the use of the game, providing that the game numbers were maintained.[92]

After the founder's passing, the plaintiffs, three of the founder's other children, and also beneficiaries under the trust, claimed that the lease of the trust's assets to Jacobus was prejudicial as it was not market related, which led to financial losses for the trust. On this basis, the plaintiffs claimed damages from the trustees.[93]

Of significance for present purposes was the testimony of the second defendant, Van Loggenberg, who indicated that the founder often intimidated the trustees when the trust business was discussed and, in particular, that they were so intimidated when the terms of the lease with Jacobus had been considered. She testified that she and the other trustees had followed the founder's wishes and had failed to exercise their own discretion in determining whether the lease agreement was in the interest and to the benefit of the trust and its beneficiaries. [94]

The principal defence raised on behalf of the defendant trustees was simply that the trust deed empowered them to enter into agreements that favoured one

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89 Para 2.3.

90 Para 2.1.

91 Para 2.2.

92 See the decision of the trustees in para 3.

93 Para 3.3. In addition to damages, the plaintiffs sought an annulment of the agreements with Jacobus and the removal of the trustees from office.

94 Paras 9.1 and 9.2.

beneficiary over another as this fell within their discretionary prerogative.[95] The court rejected this argument and held that, upon a proper construction of the trust deed, the founder's intention was not to favour one beneficiary at the expense of another.[96] An application for leave to appeal followed, but was refused.[97]

However, and significantly for present purposes, the court proceeded to hold in the alternative, and in the event that it was incorrect in its interpretation of the trust deed, that the trustees had breached their fiduciary duty by failing to act in an independent and impartial manner. The court's strong reliance on this failure is borne out in both the judgment in the action and the judgment refusing leave to appeal as follows:

> "Selfs al sou gesê kan word dat die voorbehoudsbepaling aan die trustees 'n diskresie bied om na willekeur met die bates te handel, het nóg Loggenberg nóg Du Toit getuig dat, ten tye van die neem van die tersaaklike besluit in Augustus 2001, die trustees hoegenaamd behoorlik die aangeleentheid oorweeg het en daarna 'n deurdagte besluit geneem het. Inteendeel is dit duidelik dat die besluit primêr deur die oorledene geneem is, en dat die ander trustees soos marionette bloot daarmee saamgestem en ingeval het sonder om 'n onafhanklike diskresie uit te oefen. Geen uitoefening van 'n diskresie het dus hoegenaamd geskied deur enigeen van die eerste, tweede en vierde verweerders nie. [Jacobus] het verkies om nie te getuig nie. Uit [sy] aanvaarding van die besluit en die afwesigheid van enige getuienis tot die teendeel kan aanvaar word dat ook [hy] bloot berus het in die besluit van die oorledene. Waarom sou [hy] nie in die besluit berus het nie: hy is immers enorm daardeur bevoordeel."[98]

and

> "Self al sou ek verkeerd wees in my vertolking van paragraaf 5 van die trustakte, was die verweerders steeds, *qua* trustees, regtens verplig om behoorlik en verantwoordbaar die sake van die Trust in belang van die trustbegunstigdes te bestuur. Dit het hulle, op hul eie getuienis, nalatiglik versuim om te doen. Trouens, soos bevind, en soos toegegee deur mnr. Coetzee [counsel for the defendants], het hulle eenvoudig geen onafhanklike

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95 Para 14.

96 Paras 14.1-14.4.

97 The judgment in the application for leave to appeal, which was refused, is reported electronically on the Saflii database as *Wiid v Wiid* (1571/2006) [2012] ZANCHC 9 (30 April 2012) <http://www.saflii.org/za/cases/ZANCHC/2012/9.html> (accessed on 08-09-2018) ("*Wiid leave to appeal*").

98 *Wiid* para 14.2.

> diskresie uitgeoefen tydens die besluitnemingsproses met die sluit van die huurkontrakte nie, en het hulself laat intimideer deur die oorledene, en bloot sy wil klakkeloos gevolg."[99]

On this basis, the court held that the relevant trustees had failed in their fiduciary duties as set out in section 9 of the TPCA and that they were to be held personally liable for the loss suffered by the trust.[100]

The practical effect of trustees failing to act independently in the administration of the trust is borne out by the outcome in the *Wiid* matter. The court's reasoning in this respect should be supported as it enforces the fiduciary proposition as the basis for a trustee's duty to remain independent once a valid trust has been established.

The importance of the office of trusteeship as the source of a trustee's fiduciary duty is illustrated by the outcome of *Griessel NO v De Kock* ("*Griessel*").[101] Therein the SCA held that the role of a trustee called for the exercise of a fiduciary duty owed to all the beneficiaries, irrespective of whether they had vested rights or were contingent beneficiaries whose rights would only vest on the happening of some uncertain future event.[102] The facts of the matter were as follows.

In 1999, two sisters established an *inter vivos* trust. The trust in question held all the shares in a private company, which in turn had as its sole asset a farm situated within a game reserve in Mpumalanga. The trust was a discretionary trust, in the sense that the trustees had the power to select beneficiaries from time to time from amongst those described in the trust deed as "potential beneficiaries". The trust deed contained the following provision:

> "The Trustees shall have the power, in their entire discretion from time to time and at any time to pay to, or to apply the whole or any part of the income of the trust fund for the general advantage of anyone or more of the beneficiaries as the Trustees may decide, and in such proportions and from such source as the Trustees may determine, and any income so paid or applied shall accrue to the beneficiary."[103]

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99 *Wiid leave to appeal* para 4.

100 *Wiid* para 15.5.

101 2019 5 SA 396 (SCA).

102 Para 18.

103 Clause 5.2 of the trust deed, judgment para 10.

Significantly, all the "potential beneficiaries" were afforded the right to visit the farm with their families on vacation on a rotational basis.[104]

A dispute developed between one of the potential beneficiaries, Harold de Kock ("Harold") and the trustees in relation to the commercial development of the farm. The dispute gave rise to significant acrimony between the parties and, initially, the trustees adopted an amendment of the trust deed removing Harold as potential beneficiary altogether.[105] Litigation followed and was settled on the basis that the removal of Harold as potential beneficiary was regarded as "of no force and effect and invalid".[106] However, the privilege of vacationing on the farm on a rotational basis was still refused to Harold, but was afforded to the other potential beneficiaries.

Aggrieved, Harold again approached the High Court in Pretoria effectively seeking a reinstatement of the right to vacation on the farm and the removal of the trustees of the trust. The court of first instance ordered that Harold be afforded equal access and enjoyment of the farm but stopped short of removing the serving trustees. The trustees applied to the SCA for leave to appeal (leave having been refused by the court of first instance).

The SCA directed that oral argument be heard in relation to the application for leave to appeal,[107] but that the parties be prepared, if called upon to do so, to present oral argument also in respect to the merits of the matter. The judgment is significant in the manner in which it approached the trustees' obligations to the beneficiaries. In holding that the trustees unfairly discriminated against Harold in

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104 The farm in question was situated near Pilgrims Rest in Mpumalanga. Pilgrims Rest is a small museum town in Mpumalanga and a protected provincial heritage site. See https://www.pilgrims-rest.co.za/ (accessed 23-12-2019). In view of the significant litigation that ensued, it may be inferred that the farm is an attractive vacation destination.

105 Para 3.

106 Para 3.

107 Section 17(2)(d) of the Superior Courts Act 10 of 2013, provides that:

(d) The judges considering an application referred to in paragraph (b) may dispose of the application without the hearing of oral argument, but may, if they are of the opinion that the circumstances so require, order that it be argued before them at a time and place appointed, and may, whether or not they have so ordered, grant or refuse the application or refer it to the court for consideration.

Sub-section (b) refers to an application for leave to appeal made to the SCA in the event that such an application to the court *a quo* was unsuccessful.

refusing him the privilege to vacation on the farm, the court emphasised the fiduciary obligation owed by the trustees:

> "The role of a trustee in administering a trust calls for the exercise of a fiduciary duty owed to all the beneficiaries of a trust, irrespective of whether they have vested rights or are contingent beneficiaries whose rights to the trust income or capital will only vest on the happening of some uncertain future event. While discrimination on the basis of need may, under certain circumstances, be justified by the needs of a particular beneficiary, the trustees did not advance 'need' as the reason for treating the first respondent less favourably. It is clear from the averments made in the affidavits and the tenor of the attorneys' correspondence that he was regarded as obstructive and contrarian. That may be so, but that does not suffice as justification for treating him less favourably."[108]

On this basis the SCA ordered that the trustees reinstate Harold's equal access to the enjoyment of the farm.[109] The *Griessel* matter illustrates the importance of the *quasi*-public nature of the office of trusteeship. It was common cause in that matter that the trust was a discretionary trust, in the sense that the trustees had the freedom to select beneficiaries from listed "potential beneficiaries". However, the intercession of the court to the effect that the trustees were not permitted to discriminate against one such potential beneficiary without a justifiable basis, on account of the fiduciary duty owed, underscores the *quasi*-public nature of the office of trusteeship. It is submitted that there can be no objection to a founder, in his personal capacity and prior to his death, discriminating in favour of one of his children by affording preferential treatment or privileges. In those circumstances the relationship is a purely private one. However, once assets are placed in trust the nature of the relationship changes to a *quasi*-public one on account of the nature of the office of trusteeship. As the outcome in the *Griessel* judgment illustrates, it is this public nature that accounts for the principle that trustees may not unreasonably discriminate against a particular beneficiary. It is therefore clear from this judgment that the fiduciary duty of trustees flows from their office and it follows that it is on account of the occupation of this office that trustees are required to bring an independent mind to bear upon the administration of the trust.

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108 Para 19.

109 Para 26.

5 4 The joint-action rule and trustee independence

As illustrated above, a trustee's duty to remain independent is a facet of his or her fiduciary duty.[110] In a valuable contribution to the subject of trustee independence in the context of co-trusteeship, Du Toit notes that the duty of independence:

> "essentially obliges a trustee, save when dealing with prescriptive matters of law or matters of a purely administrative nature, to bring independent judgment to bear *when participating in the decision-making processes of trust administration*."[111]

and that

> "compliance with the duty of independence ensures commensurate compliance with one of the facets of a trustee's *fiduciary duty*."[112]

This sentiment is consistent with the principles of the fiduciary proposition and in my view correctly explains a trustee's duty of independence once a valid trust has been established.[113]

However, in the context of co-trusteeship, and the obvious duty on trustees to remain independent from each other, Du Toit proceeds to suggest that this facet may further be explained on the basis of the so-called "joint-action rule".[114] The joint-action rule dictates that, in the absence of a contrary provision in the trust deed, the trustees must act jointly if the trust estate is to be bound.[115]

The application of the joint-action rule in South African trust law is uncontroversial and was once again confirmed in *O'Shea NO v Van Zyl*,[116] where the SCA held that,

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110 See part 3 3 2 in Chapter 3.

111 Du Toit (2009) *THRHR* 641 (emphasis added).

112 642 (emphasis added).

113 See part 3 3 2 The fiduciary proposition in Chapter 3.

114 Du Toit (2009) *THRHR* 642.

115 *Nieuwoudt NO v Vrystaat Mielies (Edms) Bpk* 2004 3 SA 486 (SCA) para 16 (Harms JA for the court). See also, *Goolam Ally Family Trust v Textile, Curtaining & Trimming (Pty) Ltd* 1989 4 SA 985 (C) 988D-E; *Hoosen v Deedat* 1999 4 SA 425 (SCA) para 23; *Erwee v Erwee* 2006 1 All SA 626 (O) 630J; *Thorpe v Trittenwein* 2007 2 SA 172 (SCA) para 9.

116 2012 1 SA 90 (SCA).

in order to bind a trust, "trustees must act jointly unless the trust deed provides otherwise".[117]

Du Toit's submission that the joint-action rule obliges trustees to bring independent judgement to bear on trust matters represents a departure from the fiduciary proposition as the theoretical underpinning of the duty of independence and is expressed as follows:

> "Trust administration is more often than not conducted by co-trustees. In this regard, South African trust law adheres strictly to the so-called 'joint-action rule' that requires co-trustees to act collectively in the exercise of their powers and the performance of their duties. The joint-action rule applies not only to important trustee decisions (for example, regarding the alienation or burdening of trust property), *but in respect to all trust matters*. By necessary implication, the *joint-action rule obliges each individual co-trustee to participate actively in and, therefore, to bring independent judgment to bear on the decision-making processes of trust administration*."[118]

Du Toit's argument is accordingly based on the premise that the joint-action rule is not limited to so-called "external acts",[119] but that the rule applies to *all* trustee conduct, including internal administration.[120]

This view finds support in the matters of *Smit v Van de Werke* ("*Smit*")[121] and *Coetzee v Peet Smith Trust* ("*Coetzee*"),[122] where it was respectively held that the trustees were to act jointly in the exercise of the power of assumption and in the passing of resolutions in the absence of a provision to the contrary contained in the trust deed.

While it is correct that, absent a provision in the trust deed to the contrary, trustees are required to act unanimously in the conduct of internal business, it is

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117 97B-C. See also, *Nieuwoudt NO v Vrystaat Mielies (Edms) Bpk* 2004 3 SA 486 (SCA).

118 Du Toit (2009) *THRHR* 642 (emphasis added). See also, Du Toit (2013) *Trust Law International* 18.

119 Cameron et al distinguish between internal administrative acts, on the one hand, and external acts or business with outsiders. See, E Cameron, M de Waal & P Solomon *Honoré's South African Law of Trusts* 6 ed (2018) 375-387.

120 See, Du Toit (2013) *Trust Law International* 18; *Coetzee v Peet Smith Trust* 2003 5 SA 674 (T) 680F.

121 1984 1 SA 164 (T).

122 2003 5 SA 674 (T).

submitted that this duty is not founded upon the joint-action rule, but is rooted in their simultaneous occupation of the office of trusteeship.

An analysis of the theoretical underpinnings of the joint-action rule illustrates that it operates only in respect of business with outsiders, with the concomitant conclusion of obligations for the trust estate, but not in respect of the internal management of the trust.

The rule accordingly does not provide an explanation for the requirement for trustees to act independently in the internal administration of the trust. This will become apparent from the discussion that follows.

5 4 1 The type of joint ownership applicable to trusts

In *Land Bank v Parker*,[123] Cameron JA explained that the joint-action rule derives "from the nature of the trustees' joint ownership of the trust property. Since co-owners must act jointly, trustees must also act jointly".[124]

While it is now established that the joint-action rule is rooted in the nature of the joint ownership by trustees, the nature of this type of ownership was until recently unclear. De Waal proposed that the type of co-ownership among co-trustees in respect of trust property is similar to the concept of "joint tenancy" in English law.[125]

"Tenancy" in this context must be understood as denoting ownership and should not be confused with any landlord-tenant relationship.[126] In essence, the principle of joint tenancy provides that the entire interest in the trust property is vested simultaneously in all the trustees and that the trustees are deemed to form "a collective entity – one composite person".[127]

The concept can be fully explained as follows:

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123 2005 2 SA 77 (SCA).

124 Para 15. See also the judgment of Van Dijkhorst J in *Coetzee v Peet Smith Trust* 2003 5 SA 674 (T) and Honoré "Trust" in R Zimmerman & DP Visser (eds) *Southern Cross – Civil Law and Common Law in South Africa* (1996) 854 n 39.

125 MJ de Waal "The strange path of trust property at a trustee's death: theory and practice in the law of trusts" (2009) *TSAR* 84.

126 According to Riddall *Land Law* (2003) 170, the term in this context derives from the term "tenant" in the old context of tenure. As pointed out by De Waal (2009) *TSAR* 84 87 n 14, there is also an obvious link with the Latin term *teneo*, meaning "to hold".

127 K Gray & S Gray *Elements of Land Law* 5 ed (2009) 914 n 2.

> "The essence of joint tenancy consists in the theory that each joint tenant is wholly entitled to the whole of the interest which is the subject of co-ownership. The key to understanding joint tenancy is the realisation that no joint tenant holds any specific or distinct *share* himself, but each is (together with the other joint tenant or tenants) invested with the totality of the co-owned interest."[128]

Joint tenancy is therefore distinguishable from the established forms of co-ownership recognised in South African law. In South African law, co-ownership has been recognised as either normal or free co-ownership ("*vrye mede-eiendom*") or bound common ownership ("*gebonde mede-eiendom*").[129] As explained by De Waal,[130] free co-ownership originates in Roman law and exists in the normal course of business where two or more persons become co-owners of a thing, for example where two parties jointly purchase a thing. Bound common ownership, on the other hand, originates in Germanic law and exists where persons become co-owners of a thing by virtue of a special relationship between them, for example, a partnership or a marriage in community of property.

A central feature of both these traditional modes of co-ownership is that each owner holds a share of the property or, more specifically, "undivided shares".[131] It is accordingly possible that an owner in free co-ownership could own a two-thirds undivided share in an asset with the other holding the remaining third share.[132] This is, however, not possible where property is held by virtue of joint tenancy as the entire interest in the property is then vested simultaneously in all the co-owners, to the extent that the co-owners are (in relation to third parties) in the position of a single owner.[133]

This explains what has been referred to as the "elastic" nature of ownership in trust property, as the removal of one trustee does not give rise to any formal or

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128 Gray & Gray *Land Law* 914.

129 See De Waal (2009) *TSAR* 89 and see also, PJ Badenhorst, JM Pienaar & H Mostert *Silberberg and Schoeman's the Law of Property* 5 ed (2006) 133; CG van der Merwe *Sakereg* 2 ed (1989) 378; AJ van der Walt & GJ Pienaar *Introduction to the Law of Property* 7 ed (2016) 48.

130 De Waal (2009) *TSAR* 90.

131 Van der Merwe *Sakereg* 378-394.

132 380. Note the distinction with the English form of ownership described as "tenancy in common" where the owners hold the property in undivided shares.

133 See De Waal (2009) *TSAR* 89; C Harpum *Megarry and Wade: The Law of Real Property* (2000) 475.

express transfer of ownership and the "slack in the title" is simply "taken up" by the remaining trustees.[134]

This phenomenon is known in English trust law as the "rule of survivorship" and has been said to be the "grand and distinguishing incident of joint tenancy".[135] De Waal explains the rule of survivorship as follows:

> "In its essence the rule of survivorship entails that, on the death of one joint tenant, his or her interest in the property passes to the other joint tenants by the *ius accrescendi* (right of accrual). This process defeats any provision in a joint tenant's will or the rules of intestacy and it continues until there is only one survivor, who then holds the property as sole owner."[136]

It is, accordingly, clear that the rule of survivorship depends solely on ownership being held through joint tenancy as the traditionally recognised modes of co-ownership would by necessary implication require a formal transfer of ownership between the respective trustees.[137]

Notwithstanding an initial rejection of joint tenancy by Cameron et al,[138] it now appears settled that this peculiar form of ownership has been received into South African law.

In the fifth edition of their work, Cameron et al unequivocally rejected the idea that joint tenancy has been received into South African law, but proceeded to explain that upon the death of a trustee "the ownership of the trust property … passes to the executor of the trustee's estate, and must be transferred to the surviving or new trustees".[139] However, later in the same textbook the authors, seemingly contrary to the above view, recognise the operation of the rule of survivorship and suggest that upon death a trustee:

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134 De Waal (2009) *TSAR* 91, referencing K Reid in T Smith & R Black (eds) *The Laws of Scotland: Stair Memorial Encyclopaedia* 18 (1993) para 35.

135 See Gray & Gray *Land Law* 915.

136 De Waal (2009) *TSAR* 88. See also, AJ Oakley *Megarry's Manual of the Law of Real Property* (2002) 303; Gray & Gray *Land Law* 915.

137 De Waal (2009) *TSAR* 90.

138 E Cameron, M de Waal, B Wunsh, P Solomon & E Kahn *Honoré's South African Law of Trusts* 5 ed (2002) 27.

139 27.

> "loses the ownership of any assets which the person held as trustee provided that there remains another trustee in whom they can vest by virtue of the rule of survivorship."[140]

This view also appears to be in step with what happens in practice.[141]

The initial position expounded by Cameron et al,[142] was questioned by De Waal, who showed that joint tenancy had, in fact, been received into South African law as far as ownership of trust assets is concerned. The evidence for this conclusion is indeed there: recognised models of co-ownership are unable to explain the operation of the rule of survivorship and, moreover, there is nothing inherent in the concept itself that is incompatible with South African law.[143] The observation that the rule of survivorship has been consistently applied in the context of South African trust law also reinforced the argument that joint tenancy was received into South African law as a composite part of the English trust that was introduced in the early nineteenth century.[144]

In the latest version of their work, Cameron et al have accepted that joint tenancy has been received into South African law. Further, that it accounts for the applicable property regime regarding trusts,[145] and that:

> "It appears that 'joint tenancy' as a form of co-ownership among co-trustees and the related rule that the office of trustee is conferred individually on the trustee in question, and is not transmitted to the trustee's executor, have been received in South Africa."[146]

It is submitted that it is therefore now settled that the rule of survivorship has been received into South African law.

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140 574. This statement has been retained in the latest edition of that work. See Cameron et al *Honoré* 593.

141 See also, De Waal (2009) *TSAR* n 32 where the author explains that, while no direct authority for this submission could be found, same was based on feedback received from trust law practitioners and the author's own experience. My own investigations in the form of discussions with trust practitioners and my own experience, support this submission.

142 Cameron et al *Honoré* 5 ed 27.

143 De Waal (2009) *TSAR* 92.

144 92. See also, MJ de Waal "The core elements of trust: aspects of the English, Scottish and South African trusts compared" (2000) 117 *SALJ* 548 570 n 143.

145 Cameron et al *Honoré* 32.

146 33.

5 4 2 Joint-action rule does not compel joint decision making

Returning to the concept of trustee independence and the proposition by Du Toit that the joint-action rule compels trustees to exercise independence also in the context of internal administration,[147] it is submitted that this proposition is incorrect. This is so because, as shown above, the joint-action rule has its roots in the co-ownership (in the form of joint tenancy) of the trust assets. While it therefore follows that all acts that may create an obligation with respect to the trust estate *vis-à-vis* third parties would require joint action by the trustees, the co-ownership of the trust estate does not *per se* explain the requirement to act unanimously in respect of the internal administration of the trust.

The authority cited by Du Toit for his proposition that it does, is *Coetzee*.[148]

That matter concerned the efforts of the trustees of a trust to terminate the employment of an employee who also served as a trustee. Unsurprisingly, the employee in question (the applicant in the matter) did not agree to the termination of his employment and a unanimous trustee resolution was therefore impossible.[149] Following a resolution to terminate his employment contract by the remainder of the trustees, the applicant sought a declarator that the resolution was invalid.

The question to be answered was therefore whether a decision to terminate the employment contract of the applicant could be validly taken by a majority of the trustees in office, or whether they were required to act unanimously.[150]

The trust in question was a testamentary trust and the will in terms of which it was founded did not provide that a majority decision could pass resolutions. It was argued on behalf of the applicant that the resolution to terminate his employment was invalid since the trustees were required to act jointly.

This line of argument found support with Van Dijkhorst J, who held as follows:

> "Daar is goeie gronde vir 'n reël dat trustees gesamentlik moet optree en eenparig moet beslis.
>
> Die trustgoed word normaalweg aan trustees in eiendomsreg oorgedra ... Mede-eienaars het gesamentlike eiendomsreg, gebruiksreg en beheersreg oor die mede-eiendom. Daar geld nie 'n meerderheidstem nie. Beslissinge moet gesamentlik en

147 Du Toit (2009) *THRHR* 642.

148 2003 5 SA 674 (T).

149 676A-677I.

150 676E.

> eenparig geneem word om geldig te wees in soverre meer as die *pro rata* belang van die afsonderlike mede-eienaar betrokke is ...
>
> Tensy die trustakte of testament bepalings tot die teendeel bevat is daar regtens geen rede om 'n ander reël te volg in die geval van trusts nie. Trouens die saak is sterker. Indien 'n oprigter meerdere persone aanwys om trustees te wees is dit klaarblyklik sy bedoeling dat hulle gesamentlik moet optree. Waar daar twee trustees is beteken dit eenparig. Waarom sou die oprigter dan, waar hy byvoorbeeld drie trustees aangewys het, bedoel het dat die beslissing van twee daarvan voldoende sal wees? Klaarblyklik is in so 'n geval die derde aangestel omdat sy oordeel en beslissing ook van belang geag word. Gesamentlike eenparige optrede in die vervreemding, hantering en bestuur van die trustgoed is dus 'n voorvereiste."[151]

On behalf of the respondents, it was submitted that the co-ownership of trust assets only enjoins the trustees to act jointly in respect of the alienation or burdening of the trust assets and that the rule requiring joint action did not extend to the internal administration of the trust. This argument was rejected as follows:

> "Namens die respondente is betoog dat gesamentlike eenparige optrede slegs vereis word waar trustbates vervreem of beswaar word. Daar is geen gesag of logiese rede vir die stelling nie. Ondeurdagte kontrakte kan net so nadelig wees vir die trust as vervreemding van bates."[152]

Accordingly, it was held that the trust resolution terminating the applicant's employment was void.[153] As explained below, the *conclusion* that trustees are required to act unanimously with regard to the *internal business* of the trust is correct. However, this duty is not rooted in the joint-action rule but derives from the nature of the trustee office.

The analysis of the court in *Smit*[154] illustrates this point. That case revolved around the exercise of the power of assumption by a sole trustee and bears an uncanny resemblance to the *Land Bank v Parker* case, albeit that it played out nearly 20 years earlier.[155]

The *Smit* case concerned a testamentary trust in which the founder, a Mr Johannes van de Werke, appointed his surviving spouse from a second marriage

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151 678G-679C.

152 680F.

153 681D.

154 1984 1 SA 164 (T).

155 167H-168A.

and the first respondent in the application, Mrs van de Werke, together with his accountant, Mr Geyser, as trustees of the trust established in his will.

Mr Van de Werke also stipulated that there should at all times be no fewer than two trustees in office,[156] and that, in the event that any of the trustees would vacate the office, his or her place was to be taken by a partner in Mr Geyser's firm. The trust accordingly had a capacity-defining requirement akin to that highlighted in *Land Bank v Parker*. In addition, the trustees were clothed with the power of assumption.[157]

Upon the founder's death, Mrs Van de Werke and Mr Geyser assumed the office of trusteeship and managed the trust estate until Mr Geyser's resignation two years later. After Mr Geyser's resignation, his position as trustee was offered to the other partners in his firm, but all eligible candidates declined the nomination. This prompted Mrs Van de Werke to appoint a second trustee from outside Mr Geyser's firm through the purported exercise of her power of assumption.

Mr Van de Werke's children from his first marriage opposed this appointment and launched an application to have it set aside. The now obvious point, courtesy of the *Land Bank v Parker* judgment, that a trust suffers from incapacity where there is a sub-minimum of trustees in office,[158] was not directly argued. Instead, the applicants confined their attack on the capacity of the surviving trustee to exercise the power of assumption without the concurrence of another trustee. The submissions on behalf of the applicants were summarised as follows:

> "Juridies is die aanval op die tweede respondent se aanstelling voor my gerig teen die eerste respondent se mag om op haar eie en sonder die medewerking van 'n ander eksekuteur of trustee, 'n verdere trustee te assumeer. Dit word namens die applikante aangevoer dat die eerste respondent haar mag van assumpsie slegs kan ontleen aan die testament van die erflater; dat dit duidelik uit die bewoording daarvan blyk dat die amp 'n gesamentlike een is bestaande uit twee persone en dat een enkele trustee onder geen omstandighede op sy eie kan funksioneer nie. Dit sluit ook die mag van assumpsie in. Gevolglik is die tweede respondent se aanstelling en die 'Akte van assumpsie' wat in Nederland verly is, ongeldig. Dit word aan die hand gedoen dat die eerste respondente die Hof moes genader het vir die aanstelling van 'n tweede persoon as trustee om haar

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156 167B-D.

157 166F. In this context, the power of assumption refers to the power to appoint further trustees to assist with the administration of the estate.

158 *Land and Agricultural Bank of South Africa v Parker* 2005 2 SA 77 (SCA) 91E-93D.

> gebrekkige bevoegdheid aan te vul. Hierdie persoon sou slegs deur 'n Hof aangestel word met inagneming van die wense van en na oorlegpleging met die uiteindelike erfgename. Indien die eerste respondente en hierdie aangestelde trustee so sou besluit, kon hulle dan 'n derde persoon assumeer en, as hulle nie hieroor kon ooreenkom nie, sou hulle die Hof weer moes nader. "[159]

The respondents conceded that the trust deed required a minimum of two trustees in office but argued that, with regard to the power of assumption, this power was conferred upon both trustees to be exercised independently. The judgment accordingly turned on the issue of whether the power of assumption could validly be exercised by a trustee acting alone, absent such express provision in the trust deed.[160]

In arriving at its judgment, the court relied on an extract from Halsbury's *Laws of England*[161] to the effect that the power of appointment in the context of assumption is granted to the trustees as "it is annexed to their office".[162] It was accordingly acknowledged that the power of assumption derived from the *office of trusteeship* to which it was conferred and the remaining question, therefore, was whether this power could be exercised by one trustee acting alone.

In a passage reminiscent of *Land Bank v Parker*, Le Roux J held that the requirement of two trustees was indicative thereof that a single trustee could not act alone. The court held that:

> "Na my mening blyk dit duidelik hieruit dat die mag van assumpsie slegs erken word indien die erflater dit uitdruklik toeken, en, tweedens, en nog belangriker, dat waar 'n kworum-bepaling in 'n testament voorkom die oorblywende eksekuteurs (of eksekuteur) nie kan funksioneer in enige opsig, selfs nie eers om 'n ander persoon te assumeer nie, waar hulle getal te kort skiet aan die vereiste kworum."[163]

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159 168D-F.

160 168H; 171C.

161 Lord Hailsham of Marylebone (ed) *Halsbury's Laws of England* 38 4 ed (1982) para 1564.

162 171D.

163 172E.

Ultimately the court held that Mrs Van de Werke could not have exercised the power of assumption since the office of trustee was not quorate and, consequently, the appointment of the second trustee was set aside.[164]

The significance of the judgment in the *Smit* case lies therein that it acknowledges that the office of trusteeship is the source of the power of assumption and that such power is conferred upon the bearer of that office by the trust deed. The joint ownership of the trust assets was not in issue because the power to assume another trustee did not flow from the real rights held by the trustees.

This finding echoes the emphasis placed on the office of trusteeship by Honoré.[165] The public nature of the office of trusteeship is discussed in Chapter 2,[166] where it is described in view of the supervisory role that the courts and the Master play in the administration of the trust. However, for Honoré the office of trusteeship accounts for more than merely the court's supervisory role in connection with trusts. As explained by De Waal:

> "It also tells us why a trust will not fail for want of a trustee; it explains the general duties of a trustee (thus providing a link with the trustee's fiduciary position); it is a key to understanding the concept of separate private and trust estates; and it makes clear why one can have a trust without ownership necessarily having to vest in the trustee."[167]

Honoré emphasises that while the founder of the trust is its *constituent*, it is the trust deed that is its *constitution*,[168] and that a necessary implication of occupying an office is that the trustee must be loyal to the trust deed. Therefore, in circumstances such as *Smit*, the power conferred upon the office of trusteeship may only be exercised when that office is quorate.

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164 175A.

165 T Honoré "A comparative survey of the law of trusts and trust-like institutions" in *International Court of Justice. Certain Phosphate Lands in Nauru. Memorial of the Republic* of Nauru vol 1 (1990) 354; T Honoré "Obstacles to the reception of trust law? The examples of South Africa and Scotland" in AM Rabello (ed) *Aequitas and Equity: Equity in Civil Law and Mixed Jurisdictions"* (1997) 793 794; T Honoré "On fitting trusts into civil law jurisdictions" in *Oxford Legal Studies Research Paper No. 27/2008* <https://papers.ssrn.com/sol3/papers.cfm?abstract_id=1270179> (accessed 04-08-2019).

166 See part 2 4 4 in Chapter 2.

167 De Waal (2000) *SALJ* 566.

168 Honoré (2008) *Oxford University Legal Research Paper series* 27/2008 6.

The appreciation that the office of trusteeship is a unitary office therefore also accounts for trustees being required to act unanimously in the exercise of their *internal* administration. This is not as a result of the trustees' status as joint owners of the trust estate.

Accordingly, the duty for unanimity in the internal administration of the trust does not derive from the joint-action rule as suggested by Du Toit or as may appear from *Coetzee*[169] but derives from the joint occupation of the office of trusteeship. Put differently, it is the unitary office of trusteeship, through the various trustees, that exercises the powers conferred upon it by the trust deed.

Accordingly, the fiduciary proposition provides a sound framework within which a trustee's duty of independence may be explained. In brief, the nature of the relationship between the founder and trustee and the trustee and beneficiary is such that the reliance placed upon the trustee to bring an independent mind to bear upon the administration of the trust is justified. Accordingly, it follows that the duty of independence is a component of a trustee's fiduciary duty and a failure to act independently will constitute a breach thereof.[170]

5 5 Conclusion

It is now clear that there is no closed list of fiduciary duties and that it is the nature of the relationship between the parties that is determinative of whether such duties arise.

It is also significant that our courts have acknowledged that such duties may also arise where the fiduciary relationship is not innate to the peculiar relationship between the parties, but that the specific circumstances present would demand the imposition of such duties.[171] In the context of trusts, it is submitted that the relationships between the founder and trustee and trustee and beneficiary give rise to the fiduciary duty of trustees and that this duty is embodied in the office of trusteeship. It is therefore clear that the duty of independence, as a component of a

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169 2003 5 SA 674 (T).

170 Du Toit (2007) *Stell LR* 473.

171 *Robinson v Randfontein Estates Gold Mining Co Ltd* 1921 AD 168; *Phillips v Fieldstone Africa (Pty) Ltd* 2004 3 SA 465 (SCA); *Volvo (Southern Africa) (Pty) Ltd v Yssel* 2004 6 531 (SCA).

singular fiduciary duty, is foisted upon the trustee on the basis of his occupation of that office.

It has further been argued that the joint-action rule is not the source of the duty of independence, since this rule is rooted in the joint ownership of the trust assets. While the specific form of joint ownership in question compels trustees to act jointly in establishing obligations that bind the trust estate, there is no reason to hold that they are also so bound in the internal administration of the trust.

Instead, it is submitted, the obligation to act jointly in the internal administration of the trust, such as the passing of a resolution, is a function of the collective occupation of the trustee office.

This is not to say that trustees do not have an obligation to bring an independent mind to bear upon the determination of internal trust business. Questions of trustee independence are to be examined against the fiduciary proposition and, as is discussed in Chapter 6, a failure to apply the requisite measure of independent discretion may expose the trustee to a claim for breach of trust.

CHAPTER 6: SHAM AND ABUSE

6 1 Introduction

As discussed in Chapter 2, the separation of estates, and the recognition and enforcement of this separation, is a core element of the trust. It ensures the protection of the trust assets from the personal creditors of the trustees.[1] This principle is especially pronounced in the context of a civilian trust and is explicitly confirmed in the Principles of European Trust Law[2] and the Hague Convention on the Law Applicable to Trusts and on their Recognition.[3]

In the civilian context, the separation of estates is achieved without recourse to the "dual ownership" developed in equity, but through the recognition of a separate trust estate, distinct from that of the founder.[4] The existence of this separate trust estate has been offered as a retort to allegations that civilian trusts are not "proper" or "real"[5] trusts but merely rise to the level of "trust-like institutions"[6] or "so-called trusts".[7]

The effect of recognising that the trustees have an estate separate from their personal estates, or that of the beneficiaries, is to afford the trustees limited liability in much the same manner that separate juristic personality does.[8] This effect of limited liability has no doubt contributed to making trusts attractive vehicles to protect

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1 See the text below n 99 in Chapter 2. See also, MJ de Waal "The core elements of the trust: aspects of the English, Scottish and South African trusts compared" (2000) 117 *SALJ* 548; GL Gretton "Trusts without equity" (2000) 49 *Int Comp LQ* 599; MJ De Waal "In search of a model for the introduction of the trust into a civilian context" (2001) 12 *Stell LR* 63; MJ de Waal "The abuse of the trust (or: 'going behind the trust form'): the South African experience with some comparative perspectives" (2012) 76 *RabelsZ* 1078.

2 Art 1(1).

3 (Adopted on 1 July 1985, entered into force 1 January 1992) art 2.

4 See part 2 3 in Chapter 2.

5 See F Sonneveldt "The trust – an introduction" in F Sonneveldt & HL van Mens (eds) *The Trust: Bridge or Abyss between Common and Civil Law Jurisdictions?* (1992) 1 and JH Langbein "The contractarian basis of the law of trusts" (1995) 105 *Yale LJ* 625 669.

6 DJ Hayton "The Hague convention on the law applicable to trusts and on their recognition" (1987) 36 *Int Comp LQ* 260 262.

7 DJ Hayton "Trusts" in DJ Hayton, SCJJ Kortmann, AJM Nuytinck, AVM Struycken & NED Faber (eds) *Vertrouwd met de Trust: Trust and Trust-like Arrangements* (1996) 3.

8 See the text below n 99 in Chapter 2.

assets or further business interests.[9] However, as is also encountered in the realm of corporate law, the limited liability afforded by trusts is open to abuse by trustees, founders and beneficiaries alike to the prejudice of third parties.

This possibility was acknowledged in *Land Bank v Parker*,[10] where the court suggested that trust law may require development in order to guard against abuse:

> "It may be necessary to … extend well-established principles to trusts by holding in a suitable case that the trustees' conduct invites the inference that the trust form was a mere cover for the conduct of business 'as before', and that the assets allegedly vesting in trustees in fact belong to one or more of the trustees and so may be used in satisfaction of debts to the repayment of which the trustees purported to bind the trust. Where trustees of a family trust, including the founder, act in breach of the duties imposed by the trust deed, and purport on their sole authority to enter into contracts binding the trust, that may provide evidence that the trust form is a veneer that in justice should be pierced in the interests of creditors".[11]

On the strength of this *dictum*, South African courts have sought to develop the law of trusts in order to guard against the abuse of the trust.[12]

In this chapter the mechanisms developed to look beyond the trust form are examined. Central to this examination is the distinction between deeming a trust a "sham" and therefore to conclude that no trust was established, and justifying "going

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9 See E Nel *The Business Trust and its Role as an Entity in the Financial Environment* LLD dissertation, NNMU (2012) 101. It was this advantage of the trust that has earned it the description of "cornerstone of the unincorporated company" in English law. Manchester explained as follows:
"The property of the company was vested in trustees who were required to further the covenants which were set out in the deed of settlement. In this way it was possible to provide both for the company to sue and be sued and for the transferability of shares. It was possible even to provide for a form of limited liability, at least as between the partners."
AM Manchester *A Modern Legal history of England and Wales 1750 – 1950* (1980) 350, quoted by R Harris *Industrialising English law: Entrepreneurship and Business Organisation 1720 – 1844* (2000) 147.

10 2005 2 SA 77 (SCA).

11 Para 37.3.

12 See as examples *Badenhorst v Badenhorst* 2006 2 SA 255 (SCA); *First Rand Limited t/a First National Bank v Britz* ZAGPPHC 20-07-2011 case no 54742/09; *Van Zyl NNO v Kaye NO* 2014 4 SA 452 (WCC); *WT v KT* 2015 3 SA 574 (SCA); *REM v VM* 2017 3 SA 371 (SCA).

behind the trust" (or, as is argued, "disregarding the trust estate")[13] in circumstances where the trust form has been abused.

With regard to "sham" trusts, it is argued that the sham doctrine (and its South African counterpart) is not equipped to explain those instances where, owing to a hidden subjective intention on the part of the founder, no trust is established. Instead, the principles underlying the establishment proposition are offered as a more suitable alternative for holding that no trust was established.

In respect to those instances justifying the disregard of the trust estate, the analysis of the Western Cape Division of the High Court in *Van Zyl NNO v Kaye NO* ("*Van Zyl v Kaye*")[14] is compared to the, fairly recent, conclusions reached by the SCA in *WT v KT*[15] and *REM v VM.*[16]

It is argued that the analysis in *Van Zyl v Kaye* is to be preferred as it more closely resembles the underpinning of the fiduciary proposition which, it is submitted, should form the basis upon which future questions of disregarding the trust estate are to be considered.

Therefore, in this chapter, the establishment and fiduciary propositions developed in Chapters 3, 4 and 5 are applied to the contemporary difficulty of identifying and dealing with the abuse of the trust form. It is submitted that these propositions provide a sound theoretical framework against which sham and abuse may be measured and offer justification for either challenging the validity of the trust or disregarding the separate estate thereof.

6 2 The distinction between holding a trust a "sham" versus "going behind the trust form"

When considering questions of so-called "sham" trusts and "abuse" permitting a disregarding of the trust's estate, it is crucial to draw and maintain a clear distinction between these concepts which are approached from two different theoretical perspectives.[17]

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13 See part 6 2 below.

14 2014 4 SA 452 (WCC).

15 2015 3 SA 574 (SCA).

16 2017 3 SA 371 (SCA).

17 De Waal (2012) *RabelsZ* 1078.

The use of the term "sham" in relation to a trust has been the subject of much criticism.[18] For example, De Waal argues convincingly that there is a conceptual distinction to be drawn between sham situations, on the one hand, and the abuse of trusts, on the other.[19] As he correctly points out, in the case of a sham the question is whether the trust was validly established and the emphasis falls on the requirements for the creation of a valid trust. This distinction received judicial approval in *Van Zyl v Kaye* as follows:

> "it [is] necessary to highlight that establishing that a trust is a sham and 'going behind the trust form' entail fundamentally different undertakings. When a trust is a sham, it does not exist and there is nothing to 'go behind'".[20]

In contrast, the concept of "abuse" relates to the misuse of the separate estate afforded by trusts. In such a case, the enquiry proceeds from the premise that there is a valid trust, but that the effect of limited liability afforded through the separate estates are abused. The question, therefore, is whether the abuse warrants a court to disregard the separate estate of the trustee (that is, separate from the latter's personal estate) and hold that the trust assets be applied for a particular purpose or – albeit somewhat controversially, as pointed out by Du Toit et al[21] – that they in reality vest in a different estate (that is, the trustee's personal estate).[22] However, in what follows – for the sake of convenience of expression – reference will throughout be made to the "separate estate of the trust". Note, however, that this expression refers to the estate that the trustee holds separately from his or her personal estate.

It is trite that a trust is not a separate juristic person and, as such, it is submitted that the terms "piercing" or "lifting" the "veneer" or the "veil" of the trust, or "going behind the trust" is inappropriate as there is, strictly speaking, no juristic personality to "pierce", "lift" or "go behind". The abuse that is to be avoided relates to the

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18 J Palmer "Dealing with the emerging popularity of sham trusts" (2007) *NZ LR* 81; De Waal (2012) *RabelsZ* 1078; L BoHao "There is no such thing as a sham trust" (2013) 44 *VUW LR* 115; E Nel "Two sides of a coin: piercing the veil and unconscionability in trust law" (2014) 35 *Obiter* 570.

19 De Waal (2012) *RabelsZ* 1098.

20 *Van Zyl NNO v Kaye NO* 2014 4 SA 452 (WCC) para 16.

21 F du Toit, B Smith & A van der Linde *Fundamentals of South African Trust Law* (2019) 147.

22 De Waal (2012) *RabelsZ* 1098.

separate estate of the trust and the use thereof to achieve what the law would otherwise not countenance. Accordingly, it is suggested that the correct term for this form of relief is "disregarding the separate estate" of the trust.

In what follows, the concepts of a sham trust and an abuse which merits disregarding the separate estate of a trust are critically evaluated within the context of the independence duality and the establishment and fiduciary propositions first identified in Chapter 3.[23]

It is suggested that the "sham doctrine" in common-law jurisdictions and its counterpart in South Africa, the "simulation doctrine", are ill-suited to the law of trusts and as such should be avoided. Instead, it is argued that the establishment proposition provides a sound theoretical basis upon which the validity of a trust can be determined in scenarios where the founder merely simulated the establishment of a trust.

Recent developments in disregarding the trust estate are also examined and it is submitted that the development of this form of relief will benefit from the application of the fiduciary proposition.

6 3 There is no such thing as a "sham trust"

The debate about the appropriate use of the term "sham" in respect to trusts has only, perhaps somewhat surprisingly, developed and intensified fairly recently.[24] Proponents of the use of the term "sham" in respect to trusts argue that it correctly encapsulates the position where the apparent creation of the trust was intended to merely mislead,[25] whereas others argue that the sham doctrine is incompatible with the basic tenets of trust law.[26]

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23 See part 3 3 in Chapter 3.

24 See Palmer (2007) *NZ LR* 81; Nel (2014) *Obiter* 570; IM Shipley "Trust assets and the dissolution of a marriage: a practical look at invalid trusts, sham trusts, and piercing the veneers of trusts/going behind the trust form" (2016) 3 *Merc LJ* 508; D Mallon "A critical analysis of sham trusts" (2017) 20 *Trinity C LR* 162.

25 M Conaglen "Sham trusts" (2008) 67 *CLJ* 176; Mallon (2017) *Trinity C LR* 162.

26 Palmer (2007) *NZ LR* 81; De Waal (2012) *RabelsZ* 1078; BoHao (2013) *VUW LR* 115.

The sham doctrine is attributed to Diplock LJ who, in the 1967 case of *Snook v London and West Riding Investments Ltd* ("*Snook*"),[27] a case involving a hire-purchase agreement, said in connection with the word "sham" that:

> "As regards the contention of the plaintiff that the transactions between himself … and the defendants were a 'sham', it is, I think, necessary to consider what, if any, legal concept is involved in the use of this popular and pejorative word. I apprehend that, if it has any meaning in law, it means acts done or documents executed by the parties to the 'sham' which are intended by them to give to third parties or to the court the appearance of creating between the parties legal rights and obligations different from the actual legal rights and obligations (if any) which the parties intend to create."[28]

This dictum has acquired "canonical"[29] status and has been cited as the authoritative statement of the sham doctrine in common-law jurisdictions around the world.[30] In addition, and significant for present purposes, Diplock LJ's formulation of the sham doctrine included the following:

> "One thing I think, however, is clear in legal principle, morality and the authorities … that for acts or documents to be a 'sham', with whatever legal consequences follow from this, *all the parties thereto must have a common intention that the acts or documents are not to create the legal rights and obligations which they give the appearance of creating*."[31]

Against this background, it has become well-established that for a transaction to constitute a sham, all the parties thereto must share the intention to create the

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27 1967 1 All ER 518 (CA).

28 528.

29 Conaglen (2008) *Cambridge LJ* 177. See also *A v A* 2007 EWHC 99 (Fam) para 32.

30 See eg, (i) in England, *WT Ramsay Ltd v Inland Revenue Commissioners* [1982] AC 300 337; *Welsh Development Agency v Export Finance Co Ltd* [1992] BCLC 148 (CA); *Painter v Hutchison* [2007] EWHC 758 (Ch) 110; (ii) in Australia, *Sharrment Pty Ltd v Official Trustee in Bankruptcy* (1988) 82 ALR 530 537; *Equscorp Pty Ltd v Glengallan Investments Pty Ltd* [2004] HCA 55 (2004) 218 CLR 471 para 46; (iii) in New Zealand, *Bateman Television Ltd v Coleridge Finance Co. Ltd.* [1969] NZLR 794 821 (CA); *Official Assignee v Wilson* [2006] 2 NZLR 841 para 52; (iv) in Canada, *Minister of National Revenue v Cameron* [1974] SCR 1062 1068; and (v) in Jersey, *Gruppo Torras SA v Al-Sabah* [2004] 1 WTLR 1 para 54.

31 *Snook v London & West Riding Investments Ltd* [1967] 1 All ER 518 (CA) 528 (emphasis added).

sham.[32] This requirement has been labelled the "common intention requirement",[33] and has been applied widely within the common-law world in cases where a trust has been alleged to be a sham.[34]

In South Africa, an article that appeared in the De Rebus journal in 2007 ignited the debate in respect of sham trusts.[35] In that article, the author, Joffe, draws attention to the importance of trustees maintaining a level of independence in the administration of the trust. Citing the Jersey case of *Rahman v Chase Bank Trust Company (CI) Ltd* ("*Rahman*"),[36] Joffe cautions against trust deeds that retain too much power over trust assets in the hands of the founder.

In *Rahman,* the founder, a Lebanese national, settled a trust in Jersey, and as founder retained significant control over the administration of the affairs of the trust. Upon his death, his wife and mother challenged the validity of the trust on primarily two bases. First, they relied on a surviving French element of Jersey law encapsulated in the maxim "*donner et retenir ne vaut*"[37] and, secondly, that Mr Rahman never had the intention to establish a *trust*.

The court granted the relief on the first ground but also held that:

> "We have to make a review of the evidence. We were unanimously satisfied that the oral evidence, together with the documentation placed before us, established clearly that from the date on which [Mr Rahman] purported to constitute the settlement he exercised dominion and control over the trustee in the management and administration of the settlement, including distributions of capital to himself, to others as gifts or loans, and the making and disposal of investments. He treated the assets comprised in the trust fund as

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32 This principle was reaffirmed and applied in both *Rahman v Chase Bank (Cl) Trust Co Ltd* [1991] JLR 103 and *Hitch v Stone* [2001] STC 214 para 69.

33 BoHao (2013) *VUW LR* 116.

34 *Shalson v Russo* [2003] EWHC 1637 (Ch); *Esteem Settlement* [2001] WTLR 641.

35 H Joffe "'Sham' trusts" *De Rebus* (January/February 2007) 25 26. *De Rebus* is the South African attorneys' journal which is published monthly. See http://www.derebus.org.za (accessed on 24-12-2019).

36 (1991) JLR 103. See the discussion of this case by P Laidlow "Shams" (2000) 12 *TACT* (available online at <http://www.tact.uk.net/review-index/sham-trusts/>) (accessed on 11-05-2019). The phrase "sham trust" came into use internationally after the Royal Court of Jersey's decision in *Rahman*.

37 Translated as: "To give and hold back at the same time does not work". See J Nigel "*Donner et retenir ne vaut*? Reflections on the retention of founder's rights" (2011) 17 *Trusts & Trustees* 451 452 (available online at <https://doi.org/10.1093/tandy/ttr073>) (accessed on 03-03-2019).

> his own and the trustee as though it were his mere agent or nominee. There was retention by [Mr Rahman]. *We are unanimously of the opinion that the settlement was a sham on the facts*, in the sense that it was made to appear to be a genuine gift when it was not. Thus, even if the court were wrong on the construction of the settlement and the impact of the maxim *donner et retenir*, the settlement would still be invalid."[38]

It was after the *Rahman* case that the term "sham trust" came into international use and which ultimately ignited the debate around the suitability of the sham doctrine to the law of trusts.[39] While the focus in *Rahman* remained on the term "sham", the above-quoted analysis with its focus on retention of control is reminiscent of the manner in which elements of the control test are applied in the establishment proposition.[40]

South African law does not subscribe to the sham doctrine as developed in the *Snook* judgment, but a similar test was formulated almost 50 years earlier in *Zandberg v Van Zyl*[41] when the Appellate Division, per Innes JA, held that:

> "Now, as a general rule, the parties to a contract express themselves in language calculated without subterfuge or concealment to embody the agreement at which they have arrived. They intend the contract to be exactly what it purports; and the shape which it assumes is what they meant it should have. Not infrequently, however (either to secure some advantage which otherwise the law would not give, or to escape some disability which otherwise the law would impose), the parties to a transaction endeavour to conceal its real character. They call it by a name, or give it a shape, intended not to express but to disguise its true nature. And when a Court is asked to decide any rights under such an agreement, it can only do so by giving effect to what the transaction really is; not what in form it purports to be."[42]

As the court pointed out, the principle enunciated can be summarised in the maxim *plus valet quod agitur quam qoud simulate concipitur*.[43] It follows that in South Africa, the test is to establish the real intention of the parties to an agreement

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38 *Rahman v Chase Bank Trust Company (CI) Ltd* [1991] JLR 103 146 (emphasis added).

39 See Palmer (2007) *NZ LR* 81; Conaglen (2008) *Cambridge LJ* 176; BoHao (2013) *VUW LR* 115 and Mallon (2017) *Trinity C LR* 162.

40 See part 4 4 in Chapter 4.

41 1910 AD 302.

42 309.

43 Translated as: "The real intention carries more weight than a fraudulent formulation (or pretence)" VG Hiemstra & HL Gonin *Trilingual Legal Dictionary* (1992), quoted by De Waal (2012) *RabelsZ* 1082.

and in what manner this intention differs from the simulated intention. This test is referred to as the "simulation test".[44]

The simulation test bears a striking resemblance to the sham doctrine. In particular, it is the true, common, intention of the parties to the agreement that is relevant. More recently, the SCA in *Maize Board v Jackson*[45] held that the correct enquiry in determining whether a contract is simulated is:

> "to establish whether the real nature and the implementation of these particular contracts is consistent with their ostensible form. In pursuit of that enquiry one must strive to ascertain, from all the relevant circumstances, the actual meaning of the contracting parties."[46]

In following this manner of enquiry, the SCA in *ABSA Ltd v Moore*[47] overruled a finding of simulation by the High Court on the basis that one of the parties did not intend to disguise the contract as something it was not.[48] It is therefore clear that the "common intention requirement", that is central to the sham doctrine, also applies to the South African simulation test.

It follows that the analysis applied in other jurisdictions regarding the sham doctrine and trusts is equally applicable to the evaluation of the simulation test as a theoretical basis for exposing illusionary trusts.

The main critic of the application of the sham doctrine to trusts is Palmer who approaches the problem from a common-law perspective.[49] For Palmer, the common intention requirement intrinsic to the sham doctrine is incompatible with the manner in which trusts are established in common law jurisdictions. In what has been termed "the Palmer argument",[50] she argues that, due to the fact that it is only the intention of the founder that is determinative of the establishment of the trust, there is no valid reason to require an alternative common intention on the part of the founder and the initial trustee for a trust to be held illusionary. She expresses this view as follows:

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44 De Waal (2012) *RabelsZ* 1082. See *Commissioner for the South African Revenue Service v NWK Ltd* 2011 2 SA 67 (SCA) para 42

45 2005 6 592 (SCA).

46 Para 8.

47 2016 3 SA 97 (SCA).

48 Para 26.

49 Palmer (2007) *NZ LR* 81; J Palmer "What makes a trust a sham?" (2008) 84 *NZLJ* 319.

50 See N Peart "Can your trust be trusted?" (2012) 12 *Otago Law Review* 56 n 27.

> "In the case of trusts … only the intention of the settlor is pertinent to the creation of a valid trust. Although no one can be compelled to act as trustee, it is a basic equitable principle that a trust will not be allowed to fail for want of a trustee. Where a trustee disclaims his or her appointment, the trust property revests in the settlor but he or she holds it upon the trust of the initial settlement because the provisional vesting in the trustee until disclaimer is sufficient to constitute the trust. Further, where there is no trustee, the court will almost always appoint one … The identification, and therefore the intention, of the trustee are irrelevant to the existence of a valid trust … A valid trust is created upon the intention of the settlor alone."[51]

and

> "If no mutuality of intention is required to create a valid trust, it is conceptually incoherent to require mutuality to create a sham trust."[52]

For Palmer, it is this unilateral nature in the establishment of the trust that is decisive in evaluating whether the sham doctrine can apply to trusts. In the passage above she emphasises that a trust will not be permitted to fail for want of a trustee and, in further support of the unilateral nature of a trust, Palmer points out that it is the intention of the founder alone that is relevant in an application for the rectification of the trust deed. In this respect, she emphasises a point by Matthews that:

> "If the court will rectify the trust document without considering the trustee's own intentions, why should it look at the trustee's intentions in considering whether to ignore a trust provision as a sham?"[53]

The opposition to the Palmer argument from a common-law perspective is based on considerations of commercial certainty and fears of inequitable results should the founder's intention alone be determinative of whether or not the trust is disregarded.[54] Mallon argues that an important reason for holding that the sham doctrine, with its common intention requirement, is the correct approach in unmasking an illusionary trust is the need for commercial certainty. He cautions

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51 Palmer (2007) *NZ LR* 81 93.

52 94.

53 P Matthews "The sham trust argument, and how to avoid it" (2007) 21 *Trust Law Int* 191 198, quoted by Palmer (2008) *NZLJ* 320.

54 Conaglen (2008) *Cambridge LJ* 190; Mallon (2017) *Trinity C LR* 178.

against the approach advocated by Palmer as this would "have drastic knock-on effects for parties linked to those transactions".[55]

For Mallon, there is a sense of security (that is, certainty) in the objective expression of the founder in establishing a trust and to submit to a proposition where the trust may be challenged on the basis of the founder's subjective intention alone:

> "would in effect subvert the law's commitment to the perceived security of the objectively ascertained meaning of bilateral transactions which goes to the heart of commercial certainty".[56]

While Conaglen accepts that a trust, in common law, may be established by unilateral act, he argues that:

> "this principle is not the focus of the sham doctrine and it does not justify the court ignoring a trust where the settlor's intention, objectively determined, was to create a trust and the trustee agreed to act on the basis of such a trust simply because the settlor subjectively and entirely secretly did not in fact intend to create it. Palmer herself recognises that 'the settlor's intention is determined objectively'. If this is so, which it is, then for reasons already discussed, a court is not at liberty to ignore the existence of that objectively determined intention, and instead privilege the settlor's unilateral subjective intention, unless it has a justification for doing so. It is not so justified unless the settlor and the trustee *both* subjectively joined in a common intention to mislead third parties. To hold otherwise would unnecessarily and unjustifiably subvert the common law's commitment to the security of the objectively ascertained meaning of bilateral transactions."[57]

He further argues that the common intention requirement of the sham doctrine serves as a necessary bulwark against inequitable consequences that may follow from the approach suggested by Palmer. For him, like for Mallon, the common intention requirement represents a balance "between the need for stability in bilateral transactions and the need to protect individuals against injustice".[58]

Conaglen echoes Mallon's argument of safeguarding certainty, stating:

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55 Mallon (2017) *Trinity C LR* 178.

56 178.

57 Conaglen (2008) *Cambridge LJ* 190.

58 188.

> "The rationale for requiring a common intention to mislead is best explained by reference to general legal principles regarding the importance of upholding the certainty of bilateral transactions."[59]

and

> "A settlor who transfers property to a trustee to hold on trust, cannot set aside the trust merely because he secretly intended to retain the beneficial interest in the property if that intention was not made apparent to the trustee. Certainly, the settlor ought not to be able to set aside the trust *vis-à-vis* the trustee, as it would be grossly unfair in the context of such a bilateral arrangement for the settlor to be able to sue the trustee for, for example, dissipating the property entirely in accordance with the stated trusts …The most important question is whether a third party ought to be able to rely on the settlor's undeclared intentions in order to treat the trust as a sham *vis-à-vis* the trustee. That question need only be posed for the answer to be clear: third parties should have no standing to deny that a trust has been validly created merely because the settlor unilaterally had 'his fingers crossed behind his back' when dealing with the trustee."[60]

This debate, and the competing submissions relating thereto, were considered in a leading New Zealand case on sham trusts, *Official Assignee v Wilson* ("*Wilson*").[61] That case concerned the insolvent estate of Mr Reynolds, who was the founder of the GM Reynolds Family Trust. Messrs Wilson and Harvey, the respondents, were the appointed trustees whereupon the trust acquired immovable property. Upon the insolvency of Mr Reynolds, his trustee in insolvency, the Official Assignee, claimed that the trust was a sham (alternatively the "alter ego" of the insolvent) and that the trust property should vest in the insolvent estate for the benefit of his creditors. The High Court of New Zealand dismissed the claim and the Official Assignee appealed to the Court of Appeal of New Zealand.

The Court of Appeal considered the sham concept and, in particular, the question of whose intention was relevant in determining the nature of the trust. In upholding the trust, it was held that it was necessary to consider first what type of trust was at issue. The court held that for a self-declaratory trust (such as a testamentary trust) only the founder's intention was relevant. However, for a trust created bilaterally between the settlor and a separate trustee (such as an *inter vivos* trust) it was

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59 188.

60 188-189.

61 [2008] 3 NZLR 45.

necessary to consider a shared intention.[62] The Court of Appeal went on to conclude that it was unable to disturb the High Court's finding that, on the facts, there was not sufficient evidence to establish the requisite sham intention on the part of the founder or trustees.[63]

The distinction between unilateral and bilateral trusts that formed the basis of the decision in *Wilson* has been criticised by Palmer[64] who argues that:

> "the idea of sham is meaningless apart from the context within which it arises. 'Sham' is no more than a descriptive label attaching to a transaction which appears to be something that it is not. Yet, it is only possible to determine whether a transaction is truly something other than it appears to be by considering what is required to be fulfilled in order for the transaction to be legitimately what it appears to be … With respect, while their Honours were correct in *Official Assignee v Wilson* to formulate the relevant elements of a sham within the context of trusts as it was being alleged, it makes no sense to differentiate between unilateral and bilateral trusts when the law of trusts recognises no such distinction in the principles relating to the formation of trusts. The elements of proving a sham trust ought to be reflective of the elements proving a trust. Whether a trust is said to be unilateral or bilateral, the law of trusts requires that the relevant intention is that of the settlor alone."[65]

I find the Palmer argument persuasive. It is intellectually coherent to evaluate the validity of a trust on the principles required to establish a valid trust. In my view, there is no logical reason to impute an additional requirement of common intention to deceive in those cases where it is not a requirement for the establishment of the trust.

Palmer also answers the fears raised by Mallon and Conaglen by pointing out that the law of estoppel provides a powerful bulwark against abuse by the trustee.[66] In circumstances where a founder intentionally deceives a trustee to enter into a trust obligation, such founder would be hard-pressed to deny the trust in circumstances where the trustee entered into the obligation on the basis of the deception. This response would apply equally in the South African context where a party who has

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62 Paras 40-41.

63 Para 95.

64 Palmer (2008) *NZLJ* 319.

65 320.

66 319. Conaglen however also acknowledges estoppel as a possible remedy guarding against abuse. See Conaglen (2008) *Cambridge LJ* 189.

acted to his or her detriment upon an objective misrepresentation by the founder may also in the appropriate circumstances raise the estoppel defence.[67]

From a common-law perspective, Palmer's approach undoubtedly holds merit. However, from a South African perspective, it is the fundamental premise of the Palmer argument, that the establishment of a trust is a unilateral act, which provides an insurmountable obstacle.

While in common law, an *inter vivos* trust may be created by unilateral declaration, this is not the case in South Africa with its civilian underpinnings.[68] The general principle in South Africa was stated by Van den Heever JA in *Crookes NO v Watson* ("*Crookes*"),[69] as follows:

> "I can think of no principle of our law according to which the individual can during his lifetime unilaterally sequester a portion of his estate and dedicate it to certain ends."[70]

Cameron et al are similarly unequivocal in their view:

> "this [statement by Van den Heever JA in *Crookes*] was followed in *Challenor's Estate v CIR*[71] and is clearly right. A donation is not binding until accepted by the donee, and a unilateral decision to abandon property is revocable until another person has taken possession of it as owner. There is no good reason why unilateral declarations should be effective in the special case where the declarer wants to create a trust, and the Supreme Court of Appeal has repeatedly applied this doctrine."[72]

The authors point out that the SCA applied this doctrine in *De Freitas v Society of Advocates, Natal*[73] where an advocate was found guilty of unprofessional conduct in that he had offered to receive clients' monies into a bank account he had opened in

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67 See, *Aris Enterprises (Finance) (Pty) Ltd v Protea Assurance Co Ltd* 1981 3 SA 274 (A) and *SA Broadcasting Corp v Coop* 2006 2 SA 217 (SCA) for an exposition on the law of estoppel in South Africa.

68 E Cameron, M de Waal & P Solomon *Honoré's South African Law of Trusts* 6 ed (2018) 166. See also DJ Hayton *Underhill & Hayton's Law relating to Trusts and Trustees* 15 ed (1995) 124.

69 1956 1 SA 277 (A).

70 298, repeating his views set out in the earlier case of *Ex Parte Kelly* 1942 OPD 265 271.

71 1960 1 SA 13 (N).

72 Cameron et al *Honoré* 166.

73 2001 3 SA 750 (SCA).

his own name. Since he was not an attorney, there was no statutory protection for the clients in the form of the Attorney's Fidelity Fund against the advocate's own appropriation of the money or in the event of his insolvency.

The reason for the bilateral requirement in establishing an *inter vivos* trust in South Africa stems from the requirement that the intention to establish a trust is to be expressed in a form that is apt to create a legal obligation.[74] This means that a testamentary trust may be established through a unilateral act, but, since an *inter vivos* trust is established by contract, and through the *stipulatio alteri*, a bilateral act is required.[75]

Palmer's argument accordingly remains inapplicable in the South African context due to the fact that, in terms of South African law, a bilateral act is a pre-requisite to establish an obligation. Therefore, and at first blush, the outcome in *Wilson* would appear to apply equally in the South African context where a unilateral act is sufficient to establish a testamentary trust, but a bilateral act is required to establish an *inter vivos* trust.

Cameron et al explain as follows:

> "If a living donor declares an intention to create a trust and to appoint X trustee, but X refuses, no trust will be created since X has not accepted the donor's offer and there is no contract between them. In this case the court has no jurisdiction to appoint a trustee other than X. The donor has simply failed to create a trust. In the case of a will, by contrast, where X declines office, the court has the power to appoint trustees in X's stead."[76]

This distinction between a testamentary and an *inter vivos* trust relates to the differing manners in which they are established. As discussed in Chapter 3,[77] it is a requirement for the establishment of a trust that the founder expresses the intention to create a trust in a mode suited to the creation of a legal obligation. In the case of a testamentary trust, this is achieved through the relevant will, whereas in the context of an *inter vivos* trust, a contract is required.

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74 *Administrators, Estate Richards v Nichol* 1996 4 SA 253 (SCA) 258. See also Cameron et al *Honoré* 159. See part 3 4 1 in Chapter 3.

75 See the text to n 122 in Chapter 2.

76 Cameron et al *Honoré* 168.

77 See part 3 4 1 in Chapter 3.

The outcome of *Wilson*, therefore, fits snugly into this conceptualisation of the manner in which trusts are established in South Africa. However, this outcome appears forced in view of the requirements for validity of trusts in common-law jurisdictions and the difficulty in applying the sham doctrine. This has led at least one commentator to call for a more flexible approach to the question of illusionary trusts.[78]

Case law has also appeared to dilute the common intention requirement. In the matter of *Autoclenz v Belcher* ("*Autoclenz*"),[79] the United Kingdom ("UK") Supreme Court arrived at a nuanced interpretation of Diplock LJ's classic statement of the sham doctrine. That matter concerned a labour dispute between Autoclenz, a company providing car-cleaning services to motor retailers, and 20 individual valeters. The litigation concerned benefits claimed by the valeters who contended that they qualified as "workers" under the prevailing minimum wage regulations.[80]

The written agreement between Autoclenz and the respective valeters recorded that the latter were "sub-contractors" who confirmed that they were "self-employed independent contractor(s)". Significantly the contract expressly provided that:

> "The Sub-contractor and Autoclenz agree and acknowledge that the Sub-contractor is not, and that it is the intention of the parties that the Sub-contractor should not become, an employee of Autoclenz …"[81]

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78 T Graham "Sham revisited: has Snook passed its sell-by date?" (2016) 22 *Trusts & Trustees* 859.

79 [2001] UKSC 41.

80 In the UK, the National Minimum Wage Regulations 1999 (SI 1999/584) adopted the definition of "worker" in section 54(3) of the National Minimum Wage Act 1998. Regulation 2(1) of the Working Time Regulations 1998 (SI 1998/1833) is materially identical to that set out tin the National Minimum Wage Act and provides as follows:

> "'worker' … means an individual who has entered into or works under …
>
> (a) a contract of employment; or
>
> (b) any other contract, whether express or implied and (if it is express) whether oral or in writing, whereby the individual undertakes to do or perform personally any work or services for another party to the contract whose status is not by virtue of the contract that of a client or customer of any profession or business undertaking carried on by the individual."

81 *Autoclenz v Belcher* [2001] UKSC 41 para 4.

The issue to be decided was therefore whether the provisions in the agreement to the effect that the valeters would not be (or become) employees of Autoclenz could be ignored on the basis that it constituted a sham. The court pointed out that, on the test set out in *Snook*, a sham required a finding that both parties intended to paint a false picture as to the true nature of their respective obligations.[82]

However, in the context of a labour relationship, where the parties are seldom bargaining on level footing, the court held that the correct principle to follow was to ascertain "the true agreement between the parties" which would be "gleaned from all the circumstances of the case, of which the written agreement is only part".[83] This approach constituted an important departure from the *Snook* test, as it was no longer required to find that both parties intended to paint a false picture of the nature of their relationship. The focus, therefore, appears, in this context, to have shifted to the common intention of the parties regarding the *nature of their relationship* as opposed to the common *intention to deceive*.

This approach bears an uncanny resemblance to the one adopted by the SCA in *Roschcon (Pty) Ltd v Anchor Auto Body Builders CC*[84] where the court reaffirmed the genuineness of the agreement as the central consideration of the test and that, in arriving at this determination "the court examines the transaction as a whole, including all surrounding circumstances, any unusual features of the transaction and the manner in which the parties intend to implement it".[85]

Notwithstanding the above, Palmer's argument is instructive as it echoes the establishment proposition in that it is the founder's intention to establish a trust, and divest himself of control over trust assets in favour of a trustee, that is determinative. This argument based on the establishment proposition holds notwithstanding the difficulties of the Palmer argument in South Africa.

Irrespective of the position one adopts on whether or not a common intention is required to establish a trust, it is settled that it remains a separate and distinct requirement for the validity of a trust that the *founder* intends to establish a *trust.*[86]

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82 Para 28.

83 Para 29.

84 2014 4 SA 319 (SCA).

85 Para 37. See also *Natal Joint Municipal Pension Fund v Endumeni Municipality* 2012 4 SA 593 (SCA) para 18.

86 Cameron et al *Honoré* 136-157.

Viewed from this perspective, it is clear that, while the co-operation of the initial trustee may be required to establish the obligation that gives rise to an *inter vivos* trust, this requirement remains secondary to the primary question, which is whether the founder intends to establish a trust in the first place. Accordingly, the argument may be made that while the acquiescence or co-operation of the initial trustee is required to establish an *inter vivos* trust, it does not follow that this intention is relevant in determining the primary question. Once it becomes clear that the founder never intended to establish a trust (which is an independent requirement for validity and a question of fact) it is irrelevant whether the obligation in terms of which the trust was purportedly established is valid.

Holding that the validity of the trust depends on the intention of the founder alone is therefore consistent with the theoretical underpinnings of the trust and the requirement that the founder divests himself of ownership and control over the trust's assets.

Where the founder lacks the intention to divest himself of the trust assets in this manner, there can be no trust, irrespective of the intention of the initial trustees. Conceptually, the intention of the founder precedes any investigation of the intention of the initial trustees and, where the founder does not intend to establish a trust, the intention of the initial trustees is irrelevant.

When the decision in *Rahman* is viewed through this prism, it becomes clear that, notwithstanding the fact that the court expressed itself in terms more suitable to the sham doctrine, the underlying argument was premised on the basic principles of the establishment proposition in that the determination of the case turned on Mr Rahman's intention to not establish a (true) trust, but rather to disguise the control he exercised over the trust assets.

For these reasons, the sham doctrine and the simulation test are unhelpful in evaluating the validity of the trust where its establishment is drawn into question and should make way for the establishment proposition.

6 4 The establishment proposition applied

The utility of the establishment proposition to unmask arrangements masquerading as trusts is underscored by the facts and outcome of two matters where South African courts have directly examined the validity of a trust. These are *Khabola v Ralitabo* ("*Khabola*")[87] and *Humansdorp Co-operative Ltd v Wait* ("*Wait*").[88]

6 4 1 *Khabola v Ralitabo*[89]

Khabola entailed a purported business venture conducted through a trust. The applicant was the founder and, together with the first to third respondents, a trustee of the Lithakali Development Trust.[90] The trust was established for the purpose of acquiring agricultural land with a view to commencing farming activities. The purchase was financed through a loan from the Land Bank together with a grant from the (then) National Government Department of Land Affairs. The arrangement was that the four trustees would contribute on a monthly basis to the repayment of the loan to the Land Bank, but at the hearing of the matter, only the applicant had made such a contribution.

Subsequently, the applicant's co-trustees sold the land to a third party,[91] who was cited in the litigation as the fourth respondent. When faced with eviction by the fourth respondent, the applicant launched an application to set aside the sale of the land by his co-trustees. In response, the co-trustees launched a counter-application seeking

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87 ZAFSHC case no 5512/2010 of 24 March 2011.

88 ECHC case no 2896/2012 of 1 November 2016. Both these judgments are unreported. The *Khabola* judgment is available from the Southern African Legal Information Institute's (SAFLII) online database at <http://www.saflii.org/za/cases/ZAFSHC/2011/62.html> (accessed on 24-12-2019). However, the *Wait* judgment is not so readily available. While I was able to obtain a copy of this judgment, I am nevertheless indebted to Smith who not only highlighted its existence, but also provided a detailed analysis of the facts of that matter and the conclusions that were arrived at. See BS Smith "Sham trusts in South Africa: *tempora mutantur, nos et mutamur in illis* (times change, and we change with them)" (2019) 136 *SALJ* 550.

89 ZAFSHC 24-03-2011 case no 5512/2010.

90 Para 1.

91 It does not appear that the applicant was a party to this agreement, nor that he had a hand in effecting the transfer thereof to fourth respondent.

an order removing the applicant as trustee, authority to wind-up the trust estate, and to dissolve the trust.

At the hearing of the application it was agreed that the court first decide the matter of *locus standi* of the parties to bring the applications against each other as they did.

In arriving at the conclusion that the parties did have such *locus standi*, the court held that the trust was simulated and that it was, in reality, a partnership:

> "Having found that the parties clearly had the formation of a partnership in mind from the onset and tacitly agreed to the applicant performing the role of a general manager, the alleged Trust seem[s] simulated. No meetings of trust[ees] were held either. Of course the partners in a partnership have a right to sue each other. The direct and substantial interest in the matter is clear in as far as everyone is concerned."[92]

On the facts, the court accordingly effectively held that the applicant (as founder) did not have the requisite intention to establish a trust, but that the parties (and by implication also the founder) in reality intended to establish a partnership. This emphasis on the intention to establish a trust is to be welcomed and echoes the premise of the establishment proposition that the founder must intend to establish a *trust* and not create some other arrangement.

However, the judgment has, justifiably, been criticised for appearing to hold that a failure to establish a trust equates to the establishment of a partnership:

> "Alhoewel die hof in die *Khabola*-saak bevind dat die bedoeling om 'n trust op te rig ontbreek en die trust dus 'n *sham* is, *is dit jammer dat dit nie as noodwendige gevolg hiervan duidelik bevind dat die trust 'n* sham *is en* ab intio *nietig is nie.* In plaas daarvan bevind die hof dat die partye 'had the formation of a partnership in mind from the onset'. Dit beteken dat die regter, na ons mening, op die oog af gedwonge voel om te bevind dat daar by alle gevalle van 'n *sham*-trust outomaties 'n vennootskap ontstaan, en dit kan tog nie.
>
> Om net eenvoudig 'n skyn- of *sham*-trust in alle gevalle as 'n venootskap te beskou is regtens onaanvaarbaar." [93]

The above approach by Vorster and Coetzee must be correct.[94] It does not follow automatically that a failure to establish a trust equates to the establishment of a

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92 Para 5.

93 A Vorster & JP Coetzee "Die geldigheidsveriestes van 'n trust opnuut ondersoek *Khabola v Ralithabo* [2011] ZAFSHC 62" (2015) 18 *PER/PELJ* 1797 1803.

partnership.[95] Their additional criticism that, in order to make a finding that the parties established a partnership, the court was required to consider and measure the arrangement established against the essentialia of partnership, also cannot be faulted.[96]

The judgment in *Khabola*, however, remains significant for its willingness to question the validity of a trust on the basis of scrutiny of the intention of the founder and underscores that such scrutiny serves as the point of departure in applying the establishment proposition.

6 4 2 *Humansdorp Co-operative Ltd v Wait*[97]

Wait is, arguably, of more value in demonstrating the utility of the establishment proposition than *Khabola* as the trust there in question was invalidated on account of the founder not affording the trustees sufficient capacity for independence.

The facts were briefly as follows. Mr Wait was the founder and co-trustee of the Wait & Wait Family Trust which was established in 2000. The other trustees were his wife, Mrs Wait, and an independent third party. The third party's independence was premised on the basis that he was neither a relative of the Waits nor a trust beneficiary. The beneficiaries of the trust were Mr and Mrs Wait and their children.

During 2009 the plaintiff, Humansdorp Co-operative Ltd ("the co-op") obtained default judgment against Mr Wait in his personal capacity for the sum of R620 000. In 2012, Mr Wait resigned as a trustee of the trust and the debt owing to the co-op remained unpaid. Later that year (judging from the case number) the co-op instituted action for the recovery of the sums owed to it by Mr Wait, against the trust. Initially, the action was directed against the trustees in their official capacities, and against Mr and Mrs Wait in their personal capacities, and later the beneficiaries of the trust were joined as further defendants on account of the interests that they had in the outcome.

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94 Smith (2019) *SALJ* 573 also supports this view.

95 International authority that suggests the existence of a partnership where a trust was invalidated should probably be understood against the particular background of that jurisdiction and the joint-stock company concept. See part 3 3 1 in Chapter 3.

96 Vorster & Coetzee (2015) *PER/PELJ* 1803-1805.

97 ECHC case no 2896/2012 of 1 November 2016.

The plaintiff's primary contention was that the trust was never validly established or had never "come into being *de jure*".[98] In this regard, reliance was placed on several provisions of the trust deed, namely:

(i) Clause 4 thereof, which provided that there would at all times be no fewer than two trustees in office and that a trustee could provide for a successor by way of testamentary provision;

(ii) Clause 9, which described the trust as a discretionary trust and stipulated that the trustees were at liberty to benefit or withhold benefits from any income beneficiary in their absolute discretion; and

(iii) Clauses 17.3 and 17.4 which provided as follows:

> "17. Administratiewe funksies en bevoegdhede van trustees
>
> ....
>
> 17.3 Die vereiste kworum vir enige vergadering van trustees sal die meerderheid van die diensdoende trustees wees, mits die houer van die vetostem waarna in sub-paragraaf 17.4 verwys word een van sodanige teenwoordige meerderheid is.
>
> 17.4 Alle besluite en optredes van die trustees sal by wyse van meerderheidstem geskied, mits die stem van [Mr Wait] van die meerderheidstemme is."[99]

(iv) Clause 21, which permitted Mr Wait to determine trustee remuneration in his will and to prescribe a formula according to which the income and capital beneficiaries would receive trust benefits after his death. Significantly, it also stipulated that were Mr Wait to employ his will in this manner, the prescripts of the will would be binding and would prevail over any decision to the contrary made by the trustees.

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98 Para 4.

99 Para 6.

Against this background, it was argued on behalf of the plaintiff that a trust was never established on account of Mr Wait reserving "to himself the absolute right to control every decision of the trustees".[100] In particular, it was argued on behalf of the plaintiff that:

(i) there was no separation of estates between the trust estate and Mr Wait's estate;[101]
(ii) the appointed trustees were unable to exercise their fiduciary duties independently on account of being subjected to the absolute dictates of Mr Wait;[102]
(iii) the trust deed did not evince an intention by Mr Wait (as founder) to be divested of control over the trust assets in favour of an independent body of trustees;[103] and
(iv) the trust deed was "ineffective because its terms did not satisfy the requirements for the creation of a valid Trust" as Mr Wait had not "dispose[d] of the so-called Trust Estate, in that it was business as before".[104]

The defendants raised three arguments in reply. First, they relied on English case law relating to sham and argued that, since there was no common intention to deceive,[105] a "piercing" of the veil was not permitted merely on account of a court's sense of equity.[106] Secondly, that a disregard of the trust as contended for by the plaintiff, would deprive the trust beneficiaries of remedies in terms of the TPCA,[107]

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100 Para 8.
101 Para 8.1.
102 Para 8.2.
103 Para 8.3.
104 Para 8.4.
105 Para 9. The case relied on was *Snook v West Riding Investments Ltd* [1967] 2 QB 786.
106 *Adams v Cape Industries PLC* [1990] Ch 433.
107 Para 11. The remedies referred to are those contained in sections 19 and 20 of the TPCA which provide that:
"**19 Failure by trustee to account or perform duties**
If any trustee fails to comply with a request by the Master in terms of section 16 or to perform any duty imposed upon him by the trust instrument or by law, the Master or any

and, thirdly, that Mr Wait was never in *de jure* control of the trust estate.[108] In this regard, it was argued that, while Mr Wait could veto any decision of the trustees, he did not have free reign over decisions that were to be made, as all decisions by the trustees required a majority of the body of trustees. Stated otherwise, Mr Wait would require the concurrence of at least *some* of the trustees to take any enforceable decisions.

Van Papendorp AJ, sitting alone, delivered a judgment in favour of the plaintiff. In arriving at the judgment, the court emphasised the measure of independence afforded to the trustees. Although it was held that "establishing independence on the part of a trustee" was not one of the *essentialia* of the trust, it was of "persuasive" value in determining whether these *essentialia* were present.[109] In echoing elements of the establishment proposition discussed in Chapter 4, it was held that the degree of independence of the trustee-complement, as gleaned from the trust deed, would determine whether the founder has a "real intention" to create a trust or whether a

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person having an interest in the trust property may apply to the court for an order directing the trustee to comply with such request or to perform such duty.

20 Removal of trustee

(1) A trustee may, on the application of the Master or any person having an interest in the trust property, at any time be removed from his office by the court if the court is satisfied that such removal will be in the interests of the trust and its beneficiaries.

(2) A trustee may at any time be removed from his office by the Master-

(a) if he has been convicted in the Republic or elsewhere of any offence of which dishonesty is an element or of any other offence for which he has been sentenced to imprisonment without the option of a fine; or

(b) if he fails to give security or additional security, as the case may be, to the satisfaction of the Master within two months after having been requested thereto or within such further period as is allowed by the Master; or

(c) if his estate is sequestrated or liquidated or placed under judicial management; or

(d) if he has been declared by a competent court to be mentally ill or incapable of managing his own affairs or if he is by virtue of the Mental Health Act, 1973 (Act 18 of 1973), detained as a patient in an institution or as a State patient; or

(e) if he fails to perform satisfactorily any duty imposed upon him by or under this Act or to comply with any lawful request of the Master.

(3) If a trustee authorized to act under section 6 (1) is removed from his office or resigns, he shall without delay return his written authority to the Master."

[108] Para 12.

[109] Para 19.

trust was simply a "means to conduct his personal affairs and as such [he] intended to create a sham".[110]

The court placed significant reliance on the passages of *Parker* to the effect that it is the "separation of ownership (or control) from enjoyment" of the trust assets that is the core idea of the trust and that, in appropriate circumstances, courts should be prepared to "pierce the veneer of the trust".[111]

On the basis of this authority, and an interpretation of the "control test" as formulated in *Badenhorst v Badenhorst*,[112] the court ultimately held that the trust in question had never been validly created and that the supposed "trust" assets were therefore liable for attachment in satisfaction of the debt owed by Mr Wait.[113]

In arriving at this conclusion, the court, in my view correctly, rejected the defence raised on behalf of the defendants to the effect that Mr Wait had, *de jure*, relinquished control over the trust estate. Central to this finding was the veto right that Mr Wait enjoyed and the fact that his concurrence was required for any decision that the trustees were to make. This, the court held, was indicative, that Mr Wait:

> "clearly displayed no intention in the Deed of Trust to create a Trust estate separate from … his control and to divest himself of the ownership and control of the Trust estate and place it in the ownership and control of independent Trustees".[114]

Reliance for this conclusion was placed on clause 4 of the trust deed, which permitted the serving trustees to appoint successors in their will as this was further evidence that Mr Wait never had the intention to "create a [t]rust estate separate from his control".[115] In addition, Mr Wait's resignation as a trustee in 2012 was regarded as irrelevant as a novation does not resuscitate an agreement that was invalid from the outset.[116]

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110 Para 20.

111 Para 22. See also Smith (2019) *SALJ* 560.

112 2006 2 SA 255 (SCA). The "control tests" and its relevance to the establishment proposition are discussed in detail in Chapter 4. See part 4 4.

113 Paras 33 and 34.

114 Para 30.

115 Para 31.

116 Para 32.

I agree with the result of the *Wait* matter, but the reliance placed on the passages of *Parker* and *Badenhorst* to the effect that a court should, in the appropriate circumstances pierce the veneer of the trust, is regrettable. This reliance serves to conflate the conceptually distinct principles of sham and abuse. In my view, the *Wait* matter stands to be approached on the basis of the establishment proposition and questions of disregarding the trust's separate estate is not directly relevant to that matter.

Smith's analysis and critique of the *Wait* judgment also echo some of the central tenets of the establishment proposition. He concurs that, since the intention on the part of the founder to establish a trust is one of the requirements of validity, it follows that, were a founder not to intend to do so, no trust would be established.[117] However, and significantly, he highlights an important distinction between holding the trust invalid on account of the founder not *intending* to establish a trust, and *failing* to establish a trust.[118]

Smith points out that, having regard to the trust deed alone, it is extremely difficult to conclude that Mr Wait did not intend to establish a trust:

> "To put it differently, the trust deed alone, and clause 17 thereof in particular, was insufficient to conclude that [Mr Wait] had not intended to divest himself of *ownership* of the trust property. On the contrary, the trust deed made it clear that ownership of the trust property was to be vested in the three trustees, and the [Mr Wait] would, *qua trustee*, become (or perhaps more correctly 'remain'), a co-owner thereof. Only an in-depth factual analysis with reference, if necessary, to the principles of ownership transfer in the law of property could prove otherwise."[119]

The more appropriate route was to consider whether, in view of the provisions of the trust deed, Mr Wait was successful in establishing a trust. Here, it is submitted, the provisions of the establishment proposition and in particular the measure of control required to establish a trust find application.

It will be recalled that the appropriate type of control that is to be considered is asset control, and in this sense the focus falls on whether the trustees have sufficient

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117 Smith (2019) *SALJ* 553.

118 573-575.

119 574-575.

control to determine the fate of the trust assets.[120] The fact that Mr Wait had therefore reserved for himself structural control (in the sense that he could appoint trustees or determine their remuneration) is in my view not relevant to the question of whether a valid trust was established.

What is relevant is that Mr Wait engineered a trust deed that gave him effective *asset* control. This is not a matter where the trustees were afforded absolute asset control, with their powers limited by the provisions of a prescriptive trust deed. In *Wait*, the founder effectively reserved for himself the power to determine the manner in which the trust assets were to be employed. This arrangement, in my view, fails the establishment proposition test and, irrespective of whether Mr Wait, subjectively, intended to establish a trust, by reserving asset control for himself he, objectively, failed to do so.

This application of the establishment proposition also accounts for the same outcome where the asset control was not reserved for the founder, but for another. Smith postulates the following, more complex, example:

> "The facts in *Wait* provided a comparatively simple matrix within which the court was able to reach its finding, because [Mr Wait] was the founder, a trustee and a beneficiary. But what if the situation had been slightly more complex? Suppose that the facts were the same, except that [Mr Wait's] father or uncle had been the founder. (This is the typical scenario where the founder simply makes a nominal donation (such as R100) to create the trust and plays no further role in the trust's administration.) Suppose, further, that it could be proved that the founder had actually transferred this donation to the three co-trustees ([Mr Wait], his wife and a third person who was neither a relative nor a beneficiary). Assume that again, as typically occurs, the trustees later purchased property from [Mr Wait], on loan account. Would the powers reserved for [Mr Wait] by clause 17 of the trust deed prevent the trust from coming into existence?"[121]

Applying the principles of the establishment proposition to these set of facts, would lead to the same conclusion. Where the founder transfers assets in trust to a set of trustees, but effectively divests the body of trustees of asset control, vesting it in a third party, no trust can be established. It does not matter that the third party in question is also a trustee. As discussed in Chapter 5, the trustees occupy one,

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120 See part 4 5 in Chapter 4.

121 576.

unitary office.[122] It is the office of trusteeship that imbues the trustees with the power to act. Where asset control is reserved for only that one person, it cannot be said that this power flows from the office of trusteeship and, consequently, it follows that the body of trustees is divested from that power. Where the power so divested is asset control, no trust is established.

Smith arrives at the same conclusion,[123] albeit based on the following statement by Cameron et al:

> "The attempt to create a trust in the strict sense may also fail because the founder fails to confer sufficient independence on the intended trustee, makes him or her instead a mere agent … or because the intention to vest property in the 'trustee' is lacking."[124]

Smith's reliance on the above passage is correct, and the passage is useful insofar as it emphasises the founder's failure to confer sufficient independence on the intended trustee. However, it is submitted that the establishment proposition provides a sound theoretical basis for holding that no trust is established, by underscoring the capacity for independence as a requirement for a trust and providing a mechanism against which trust deeds can be measured to determine whether the correct *type* and *measure* of control is afforded to the trustees.

6 5 Disregarding the trust's separate estate

It is now clear that the consideration of the validity of a trust is conceptually entirely distinct from whether the trust's separate estate is to be disregarded. A consideration as to whether a court should in the appropriate circumstances disregard the trust's separate estate, proceeds from the premise that all the requirements for the establishment of the trust have been met and that there is such a separate estate.

As highlighted above,[125] the establishment of a trust within a civilian context gives rise to two separate estates which, in turn, imbues the trust form with the capacity to

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122 See part 5 4 2 in Chapter 5.

123 576.

124 Cameron et al *Honoré* 138.

125 See part 6 2 above.

provide limited liability for the trustees.[126] Smith accurately captured the similarity between trusts and corporate entities on this score as follows:

> "Although it is trite that the South African trust is not a juristic person unless a statute clothes it with legal personality for a specific purpose, the trust, like a company or close corporation, enjoys perpetual existence and also provides limited liability to its trustees and beneficiaries in respect of debts, in a similar fashion to that enjoyed by shareholders of companies and members of close corporations."[127]

This characteristic resulted therein that trusts are increasingly employed to fill the space traditionally occupied by corporate entities. This "newer type" of trust was highlighted as a cause for concern in *Nieuwoudt NNO v Vrystaat Mielies (Edms) Bpk*[128] when established to "escape the constraints imposed by corporate law".[129]

The core idea of the trust is to separate control from benefit and it is the "rupture of the control/enjoyment divide" that invites abuse.[130] In this regard, Smith highlights that:

> "The same motivations that may induce those in control of a company or close corporation to misuse or abuse its corporate personality – by relying on the benefits of its separate existence without truly and consistently treating it as such – may, therefore, also induce trustees of a trust to breach the control/enjoyment divide (by treating trust property as their own and to 'use the trust essentially as their *alter ego'*, for example), but nevertheless to seek refuge behind the existence of the trust when it suits them."[131]

In *Parker*, it was confirmed that the courts have both the power and duty to evolve the law of trusts in order to "ensure that trusts function in accordance with principles

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126 Gretton (2000) *Int Comp LQ* 599; KG Reid "Patrimony not equity: the trust in Scotland" (2000) 8 *Eur Rev Priv L* 427; De Waal (2001) *Stell LR* 67.

127 BS Smith "Statutory discretion or common law power? Some reflections on 'veil piercing' and the consideration of (the value of) trust assets in dividing matrimonial property at divorce – Part One" (2016) 41 *JJS* 68 69. See also BS Smith "Statutory discretion or common law power? Some reflections on 'veil piercing' and the consideration of (the value of) trust assets in dividing matrimonial property – Part Two" (2017) 42 *JJS* 1.

128 2004 3 SA 486 (SCA).

129 493D-F.

130 *Land Bank v Parker* 2005 2 SA 77 (SCA) para 29.

131 Smith (2016) *JJS* 69.

of business efficacy, sound commercial accountability and the reasonable expectations of outsiders who deal with them".[132]

To achieve this objective, it may be necessary to hold that, in suitable circumstances, the:

> "trustees' conduct invites the inference that the trust form was a mere cover for the conduct of business 'as before', and that the assets allegedly vesting in trustees in fact belong to one or more of the trustees and so may be used in satisfaction of debts to the repayment of which the trustees purported to bind the trust."[133]

South African courts have increasingly acknowledged this duty to intervene where the trust form is abused.[134] However, the theoretical basis which justifies such interference remains a question of debate.[135] The debate, in particular, revolves around the source of a court's power to intercede in the event of an abuse of the trust form and the measure of abuse that would justify such interference.

6 5 1 Source of the court's power

While there is no provision in the TPCA that expressly empowers a court to look beyond the separation of control from benefit, and thereby disregard a trust's separate estate, Van der Linde has suggested that section 13 of the TPCA may allow for a court to do so in particular circumstances.[136] This section provides as follows:

> "**13 Power of court to vary trust provisions**
>
> If a trust instrument contains any provision which brings about consequences which in the opinion of the court the founder of a trust did not contemplate or foresee and which-
>
> (a) hampers the achievement of the objects of the founder; or

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132 *Land Bank v Parker* 2005 2 SA 77 (SCA) para 37.

133 Para 37.3.

134 *Van der Merwe NO v Hydraberg Hydraulics CC* 2010 5 SA 555 (WCC); *WT v KT* 2015 3 SA 574 (SCA); *REM v VM* 2017 3 SA 371 (SCA).

135 Shipley (2016) *Merc LJ* 508; A van der Linde "Whether trust assets form part of the joint estate of parties married in community of property: comments on 'piercing the veneer' of a trust in divorce proceedings" (2016) 79 *THRHR* 165.

136 Van der Linde (2016) *THRHR* 172.

(b) prejudices the interests of the beneficiaries; or
(c) is in conflict with the public interest,

the court may, on application of the trustee or any person which in the opinion of the court has a sufficient interest in the trust property, delete or vary any such provision or make in respect thereof any order which such court deems just, including an order whereby particular trust property is substituted for other property, or an order terminating the trust."

Shipley has raised two strong arguments in opposition to this submission by Van der Linde.[137] In the first instance, he points out that both the heading and wording of section 13 of the TPCA suggest that the court's powers thereunder are limited to orders in respect of the provisions of the trust deed. Therefore, so the argument goes, it is not open for a court to rely on the provisions of section 13 to make *any* order it considers just and equitable such as disregarding the separate estate of the trust.[138]

Secondly, Shipley argues that it is clear from the wording of the provision that it only applies where the undesirable consequence is brought about by a problematic provision in the trust deed, and then only where the consequences were not contemplated or foreseen by the founder.[139]

These arguments were echoed in the matter of *Harper v Crawford NO* ("*Harper*")[140] where Dlodlo J emphasised that the court's wide discretion under section 13 of the TPCA was contingent upon two jurisdictional facts:

"In order for a court to exercise this statutory power, two jurisdictional facts are required. First, the offending provision must bring about consequences which in the opinion of the court the founder did not contemplate or foresee. Second, the provision must either hamper the achievement of the object of the founder or prejudice the interests of the beneficiaries or be in conflict with the public interests. In the event that both requirements are met, the court enjoys wider powers under s 13 to vary the provisions than the court enjoyed under common law."[141]

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137 Shipley (2016) *Merc LJ* 513.

138 Shipley points out that this interpretation is also in line with the purpose of this section, as proposed in the South African Law Commission's Report on the Review of the Law of Trusts (1987) paras 12.1 to 12.9 read with annexure B514 thereof.

139 513.

140 2018 1 SA 589 (WCC). See also *Potgieter v Potgieter NO* 2012 1 SA 637 (SCA) and *Gower v Gower* 2016 5 SA 225 (SCA) paras 33-34.

141 Para 35.

This analysis of section 13 of the TPCA was affirmed by the SCA, in upholding the judgment in *Harper*.[142] In particular, the SCA, practically quoting Dlodlo J *verbatim*, reaffirmed that:

> "For a court to intervene [in terms of section 13 of the TPCA], two requirements need to be met. First, the offending provision must bring about consequences which in the opinion of the court the founder did not contemplate or foresee. Second, the provision must either hamper the achievement of the object of the founder or prejudice the interests of the beneficiaries or be in conflict with the public interest."[143]

It is therefore clear that the powers that section 13 of the TPCA confers upon courts are specific to only those instances where an undesirable consequence flows from the provisions of the trust deed that was not contemplated or foreseen by the founder, prejudice the interests of the beneficiaries or is in conflict with the public interest. This section, therefore, expands a court's common-law power to amend a trust deed and does not relate to the disregarding of a trust's separate estate.

Shipley argues that a court's power to disregard the separate trust estate stems from the common law.[144] This proposition accords with the role that South African courts play in the development of South African trust law, as highlighted in *Crookes v Watson*[145] and *Braun v Blann & Botha NNO*[146] and in line with the duty underscored in *Parker*[147] to guard against the abuse of the trust form.

In my view, the time has come to accept Shipley's argument that a court's power to disregard the separate estate of a trust stems from the common law and the duty to guard against the abuse of the trust form.[148] This much also appears from the matter of *RP v DP*[149] where it was held that:

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142 *Harvey NO v Crawford NO* 2019 2 SA 153 (SCA).

143 Para 72.

144 Shipley (2016) *Merc LJ* 513.

145 1956 1 SA 277 (AD).

146 1984 2 SA 850 (A).

147 2005 2 SA 77 (SCA) para 37.3.

148 Cameron et al *Honoré* 313 support Shipley's views in this regard.

149 2014 6 SA 243 (ECP).

> "[T]he power of piercing either the corporate or the trust veil is derived from common law and not from any general discretion a court may have. It is a function quite separate from, for instance, the exercise of discretion in making a redistribution order under s 7 of the Divorce Act 70 of 1979 …"[150]

What is however altogether unclear, is the type and measure of abuse that would justify such interference by a court, as well as the theoretical basis therefor. In what follows, I suggest that the fiduciary proposition, as a component of the independence duality model, provides the theoretical basis for such judicial intervention and also provides guidance regarding the type and measure of abuse that is relevant.

An important contribution to the debate by Smith in the context of matrimonial matters also merits discussion.[151] The above analysis, however, requires a brief consideration of the relevant case law.

6 5 2 Case analysis

The *locus classicus* in connection with disregarding the separate juristic personality of juristic persons is *Cape Pacific Ltd v Lubner Controlling Investments (Pty) Ltd* ("*Cape Pacific*").[152] In that matter, Smalberger JA explained that, although a registered company is a legal person distinct from its members, a court could in the appropriate circumstances disregard the company's separate personality in order to impose liability elsewhere for acts purportedly performed on the company's behalf.[153] In this context, the abuse of the separate juristic personality is viewed as determinative. Du Toit et al explain:

> "Piercing or lifting the corporate veil in this sense extinguishes the differentiation between the company and the person(s) in control thereof and enables the court to impose personal liability on someone (such as a company director) who abused the company's legal personality. The *Cape Pacific* case established, in particular, that a court can, where a company's legal personality is abused through fraud, dishonesty or other improper

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150 Para 31.

151 Smith (2016) *JJS* 68 93.

152 1995 4 SA 790 (A).

153 For an explanation of the principles of *Cape Pacific* and its application in the trust context, see Du Toit et al *Fundamentals* 142,

conduct, disregard that company's separate existence and attribute personal liability to the person(s) responsible for that abuse".[154]

Jordaan v Jordaan[155] and *Badenhorst v Badenhorst*[156] are two early cases that dealt with the question of whether a trust estate was to be disregarded. These were divorce cases and at issue was whether assets placed in trust were to be taken into account in making a redistribution order in terms of section 7(3) of the Divorce Act 70 of 1979 ("the Divorce Act").

That section is aimed at ameliorating an inequity that may arise in a divorce where the parties at the time of their marriage did not have the option of concluding a marriage out of community of property with the inclusion of the accrual system, which was only introduced by the Matrimonial Property Act 88 of 1984 ("the Matrimonial Property Act").[157] Section 7(3) of the Divorce Act, therefore, empowers a court in a marriage concluded prior to the enactment of the Matrimonial Property Act to order that assets of one party be transferred to the other "as the court may deem just".[158]

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154 142. See also *Cape Pacific Ltd v Lubner Controlling Investments (Pty) Ltd* 1995 4 SA 790 (A) 803H-804D.

155 2001 3 SA 288 (C).

156 2006 2 SA 255 (SCA).

157 The Matrimonial Property Act 88 of 1984 introduced a marital regime in terms of which spouses who chose to marry out of community of property could nevertheless elect to incorporate the so-called "accrual system". In terms of this marital regime, the growth in the parties' respective estates during the currency of the marriage is taken into account at its dissolution. It provides that the party whose estate had shown the least growth is entitled to half that of which the other party's growth had exceeded their own.

158 Subsections 7(3) to 7(5) provide as follows:

"(3) A court granting a decree of divorce in respect of a marriage out of community of property-

(a) entered into before the commencement of the Matrimonial Property Act, 1984, in terms of an antenuptial contract by which community of property, community of profit and loss and accrual sharing in any form are excluded; or

*(*b) entered into before the commencement of the Marriage and Matrimonial Property Law Amendment Act, 1988, in terms of section 22 (6) of the Black Administration Act, 1927 (Act 38 of 1927), as it existed immediately prior to its repeal by the said Marriage and Matrimonial Property Law Amendment Act, 1988,

Jordaan entailed a divorce in 2001 where the parties were married out of community of property in 1976. The provisions of section 7 of the Divorce Act consequently applied. During the intervening years Mr Jordaan, an estate planner, amassed a significant estate and proceeded to manage this wealth through various trusts ("the Jordaan trusts").[159]

The parties had two children, one of whom was both blind and mentally disabled, requiring Mrs Jordaan to forgo employment and devote herself fulltime to the children's care. It was therefore common cause that Mrs Jordaan was entitled to a redistribution from Mr Jordaan's estate in accordance with section 7 of the Divorce

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may, subject to the provisions of subsections (4), (5) and (6), on application by one of the parties to that marriage, in the absence of any agreement between them regarding the division of their assets, order that such assets, or such part of the assets, of the other party as the court may deem just be transferred to the first-mentioned party.

(4) An order under subsection (3) shall not be granted unless the court is satisfied that it is equitable and just by reason of the fact that the party in whose favour the order is granted, contributed directly or indirectly to the maintenance or increase of the estate of the other party during the subsistence of the marriage, either by the rendering of services, or the saving of expenses which would have otherwise have been incurred, or in any other manner.

(5) In the determination of the assets or part of the assets to be transferred as contemplated in subsection (3) the court shall, apart from any direct or indirect contribution made by the party concerned to the maintenance or increase of the estate of the other party as contemplated in subsection (4), also take into account-

(a) the existing means and obligations of the parties, including any obligation that a husband to a marriage as contemplated in subsection (3) (b) of this section may have in terms of section 22 (7) of the Black Administration Act, 1927 (Act 38 of 1927);

(b) any donation made by one party to the other during the subsistence of the marriage, or which is owing and enforceable in terms of the antenuptial contract concerned;

(c) any order which the court grants under section 9 of this Act or under any other law which affects the patrimonial position of the parties; and

(d) any other factor which should in the opinion of the court be taken into account."

[159] *Jordaan v Jordaan* 2001 3 SA 288 (C) para 24.

Act.[160] However, it remained in dispute whether the court could take account of the assets in the Jordaan trusts to determine the extent of the redistribution.[161]

In considering this question, Traverso J emphasised the virtually unfettered discretion that a court enjoys in making a redistribution order under section 7 of the Divorce Act, provided that such redistribution was just and equitable.[162]

The court had specific regard to the manner in which Mr Jordaan had managed the Jordaan trusts. Relevant in this respect were inter-trust financial transfers; distributions to the children and loans to Mr Jordaan, all without evidence of authorising trustee resolutions.[163] On this basis, the court concluded that the Jordaan trusts were Mr Jordaan's "alter ego", which conclusion was fortified by evidence suggesting that he established one of the trusts shortly prior to the institution of divorce proceedings with the aim of sequestering portions of his estate.[164]

All of this moved the court to take the estates of the trust into consideration in setting the value of the redistribution. The court, however, held that this did not amount to a piercing of the "corporate veil":

> "Vir bogenoemde redes kom ek tot die gevolgtrekking dat by die beoordeling van die vraag wat die omvang van die herverdelingsbevel moet wees, dit reg en billik is om die bates van die trusts in ag te neem. Vanweë hierdie bevinding is dit nie nodig om te besluit of dit in die omstandighede nodig is om die 'corporate veil' deur te dring nie."[165]

In *Badenhorst*,[166] the parties to the divorce action were similarly married out of community of property prior to the enactment of the Matrimonial Property Act thereby also empowering the court to apply section 7 of the Divorce Act.[167] Mrs Badenhorst accused her husband of placing his assets in a family trust in order to diminish his personal estate, thereby diminishing the sum available for any redistribution among the spouses.[168]

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160 Para 14.

161 Para 18.

162 Para 21. See also *Beaumont v Beaumont* 1987 1 SA 967 (A) 988H.

163 *Jordaan v Jordaan* 2001 3 SA 288 (C) para 29.

164 Para 33.

165 Para 34.

166 Discussed in Chapter 4.

167 Paras 2-5.

168 Paras 2-5.

The trial court held that, for the purpose of making a redistribution order, no regard should be had to the value of the assets in the family trust. However, the SCA considered it just and equitable that regard should be had to the value of the assets held in trust for the purposes of determining the value of the contribution that Mr Badenhorst was to make to the estate of his wife.

In considering under what circumstances a court should take the trust assets into account in making a redistribution order, Combrinck AJA emphasised the measure of *de facto* control exercised by one of the parties as determinative:

> "The mere fact that the assets vested in the trustees and did not form part of the respondent's estate does not *per se* exclude them from consideration when determining what must be taken into account when making a redistribution order. … To succeed in a claim that trust assets be included in the estate of one of the parties to a marriage there needs to be evidence that such party controlled the trust and but for the trust would have acquired and owned the assets in his own name. Control must be *de facto* and not necessarily *de iure*."[169]

There has been significant debate regarding whether the above conclusion amounted to the trust estate being disregarded.[170] The *dicta* in *Jordaan* to the effect that taking account of the value of the trust assets in making a redistribution did not require a piercing of the "corporate veil" suggests that Traverso J in that matter did not consider her finding to amount to the trust estate being disregarded.

In *Van Zyl v Kaye*,[171] Binns-Ward J similarly expressed the view that the finding in *Badenhorst* did not amount to a disregard of the trust estate. He stated:

> "The effect of the court order was not to hold that the trust was a sham, or to make the assets of the trust the property of Mr Badenhorst. The court also did not go behind the trust form. The decision in *Badenhorst* went to the application of ss 7(3) – (5) of the

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169 Para 9. See part 4 4 in Chapter 4 for a discussion on the "control test" alluded to in this case. For the reasons set out in part 4 4, it is submitted that references to the "control test" in *Badenhorst* is not to be equated with the traditional control test as developed in the USA to determine whether a trust was established, aspects of which have been applied in the context of the establishment proposition.

170 *Van Zyl NNO v Kaye NO* 2014 4 SA 452 (WCC); SA Hyland & BS Smith "Abuse of the trust figure in South Africa: an analysis of a number of recent developments" (2006) 1 *Journal for Estate Planning Law* 1; Smith (2016) *JJS* 68.

171 2014 4 SA 452 (WCC) para 21.

Divorce Act, rather than to any remedy for abuse of the trust form. It was left to Mr Badenhorst to decide how to make payment in terms of the court order. The judgment did not go against the trust, or render its assets exigible at the instance of Mrs Badenhorst."[172]

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[172] Para 24. Binns-Ward J relies for this analysis on dictum in *Prest v Petrodel Resources Ltd* [2013] UKSC 34. In that case the UK Supreme Court analysed the habit of the Family Courts in that jurisdiction to pierce the corporate veil by making asset transfer orders in terms of s 24(1)(a) of the Matrimonial Causes Act, 173 (which mirrors in several respects the provisions of the Divorce Act quoted above). In paragraphs 37 – 38 of that judgment, the UK Supreme Court held that:

"'37. If there is no justification as a matter of general legal principle for piercing the corporate veil, I find it impossible to say that a special and wider principle applies in matrimonial proceedings by virtue of s 24(1)(a) of the Matrimonial Causes Act 1973. The language of this provision is clear. It empowers the court to order one party to the marriage to transfer to the other property to which the first-mentioned party is entitled, either in possession or reversion. An entitlement is a legal right in respect of the property in question. The words in possession or reversion show that the right in question is a proprietary right, legal or equitable. This section is invoking concepts with an established legal meaning and recognised legal incidents under the general law. Courts exercising family jurisdiction do not occupy a desert island in which general legal concepts are suspended or mean something different. If a right of property exists, it exists in every division of the High Court and in every jurisdiction of the county courts. If it does not exist, it does not exist anywhere. It is right to add that even where courts exercising family jurisdiction have claimed a wider jurisdiction to pierce the corporate veil than would be recognised under the general law, they have not usually suggested that this can be founded on s 24 of the Matrimonial Causes Act. On the contrary, in *Nicholas v Nicholas* [1984] FLR 285, 288, Cumming-Bruce LJ said that it could not.

38. This analysis is not affected by s 25(2)(a) of the Matrimonial Causes Act 1973. Section 25(2)*(a)* requires the court when exercising the powers under section 24, to have regard to the income, earning capacity, property and other financial resources which each of the parties to the marriage has or is likely to have in the foreseeable future: The breadth and inclusiveness of this definition of the relevant resources of the parties to the marriage means that the relevant spouse's ownership and control of a company and practical ability to extract money or money's worth from it are unquestionably relevant to the court's assessment of what his resources really are. That may affect the amount of any lump sum or periodical payment orders, or the decision what transfers to order of other property which unquestionably belongs to the relevant spouse. But it does not follow from the fact that one spouse's worth may be boosted by his access to the company's

The position adopted above suggests a clear distinction between disregarding the trust estate, thereby making those same assets available to a trustee's creditors on the one hand, and merely having regard to the value of the trust assets in determining the sum to be redistributed from the relevant party's estate on the other.

Hyland and Smith, however, argue that in having regard to the trust assets in dividing matrimonial property the courts, in both *Jordaan*[173] and *Badenhorst*,[174] have disregarded the trust estate.

With regard to *Jordaan*, the authors convincingly submit that:

> "in finding the trust assets to be capable of inclusion, Traverso J did in fact 'pierce the veneer' as (i) the finding that the trusts were the defendant's *alter ego* (in consequence of the extensive investigation into the trusts' dealings) clearly implied that the trust assets were being used 'as before'; and (ii) the facts leading to such a finding could of necessity only be established after the veneer had indeed been pierced."[175]

Similarly, Smith expresses the view that the court in *Badenhorst* also proceeded to disregard the trust estate.[176] He relies on *WT v KT*[177] and the proposition that the legal principles pertaining to disregarding the trust estate have "in essence been transplanted from the arena of 'piercing the corporate veil'".[178] On this basis, Smith correctly points out that:

> "in the company law context, piercing does not of necessity require the assets of a company to be held *in law* to be those of its controllers, but merely that they, *in fact*, used those assets to promote their personal interest *as if* they were the true owners. In addition, ... it is not necessary for the judgment to 'go against' the company. Case law provides examples of the imposition of liability *only* against the controllers personally or against those persons *and* the company. It will also be recalled that piercing may take place fully or partially. In sum, in my view, even the slightest disregard of the company's separate existence in order to impose liability of this nature will constitute piercing.

> assets that those assets are specifically transferrable to the other under section 24(1)(a)."

173 Hyland & Smith (2006) *Journal for Estate Planning Law* 12.

174 Smith (2016) *JJS* 84.

175 Hyland & Smith (2006) *Journal for Estate Planning Law* 12.

176 Smith (2016) *JJS* 74.

177 2015 3 SA 574 (SCA).

178 Para 31. See, Smith (2016) *JJS* 74.

This is no different in the case of a trust."[179]

Smith further argues that similarly, where an order is made adverse to the trust's controllers and not directly against the trust estate, this is no reason to hold that the trust estate was not disregarded. In a direct reply to the views expressed by Binns-Ward J in *Van Zyl v Kaye*,[180] (to the effect that *Badenhorst* did not represent a disregard of the trust estate on account of it being left to Mr Badenhorst to decide how to satisfy the order) Smith argues as follows:

> "In *Cape Pacific*, for example, the original judgment against the company was held 'in substance and effect' to be against L, with the result that he was ordered 'to take all such steps as may be necessary' to ensure compliance therewith. This was nevertheless still regarded as an imposition of personal liability. In much the same way, the respondent in *Badenhorst* incurred a form of 'personal liability' – *i.e.* by being ordered to pay over an amount of money that was more than it would have been if the value of the trust assets had not been taken into account – that was appropriate in the context of the facts at hand. This order would not have been possible, unless the trust "veil" had been disregarded to some extent. It was only because of the respondent's abuse of the J Trust that this (albeit less intrusive) disregard was possible in the first place."[181]

It is against this background that Smith suggests that, in the actual exercising of the judicial power to disregard a trust's separate estate in divorce proceedings, a court depends not only on its common-law power but also on matrimonial property law and divorce law. However, he emphasises that this should not be understood as suggesting that the court's power in this sense is rooted in divorce legislation; for him the court's power remains rooted in common law. This should also not permit "the conclusion that considering the *value* of trust assets as part of the 'true' *value* of a divorcing trustee-spouse's estate does not amount to piercing".[182]

Smith's submissions on this point are persuasive, especially when regard is had to the fact that (as pointed out by him)[183] there could have been no question of considering the value of the trust assets had Mr Badenhorst not failed to adhere to

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179 Smith (2016) *JJS* 84.

180 2014 4 SA 452 (WCC).

181 Smith (2016) *JJS* 84. The reference to "*Cape Pacific*" is to *Cape Pacific Ltd v Lubner Controlling Investments (Pty) Ltd* 1995 4 SA 790 (A).

182 Smith (2016) JJS 92.

183 84.

the fundamental principles of trust administration. Against this *nexus* between abuse on the one hand and disregard of the trust estate on the other, Smith's interpretation of *Badenhorst* is, in my view, to be preferred.[184]

However, irrespective of whether the courts in *Jordaan* and *Badenhorst* granted the relief on the basis of the provisions of the Divorce Act or the common law in disregarding the trust estate, what is clear is that an abuse of the trust, and in particular a failure to adhere to the fundamental principles of trust administration, invites a consideration of whether trust assets are to be taken into account in aspects affecting the relevant trustee's estate.

In much the same manner, the abuse of the trust appeared to be at the forefront of the reasoning in *Nedbank v Thorpe*,[185] an insolvency matter where an application was brought for the sequestration of the respondent. At issue was the question of whether there was sufficient reason to believe that Mr Thorpe's sequestration would yield an advantage to his creditors.[186]

At the provisional stage,[187] the applicant bank contended that Mr Thorpe had established several family trusts which he used to "insulate his wealth from creditors and thereby to frustrate the efforts of his creditors to recover debts owed to them".[188] Should Mr Thorpe be sequestrated, so the argument went, it would become possible to investigate his financial affairs and locate assets in the trusts which in reality belonged to him in his personal capacity. The court granted the provisional order,

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184 This interpretation of *Badenhorst* is also supported in *RP v DP* 2014 6 SA 243 (ECP).

185 [2008] JOL 22675 (N). A provisional sequestration order was granted, and the order was eventually made final.

186 In terms of ss 10(c) and 12(1)(c) of the Insolvency Act 24 of 1936 ("the Insolvency Act"), a court may not grant a sequestration order unless "there is reason to believe that it will be to the advantage of creditors of the debtor if his estate is sequestrated".

187 The Insolvency Act distinguishes between "provisional" and "final" sequestration: A Boraine, JA Kunst & DA Burdette *Meskin on Insolvency Law Meskin on Insolvency Law* (SI 51 2018) 2-18 explain the rationale for the distinction as follows:
"The reason for this is that not only the interests of the applicant and the debtor, but also the interests of all the debtor's creditors, are affected when a sequestration order is granted ... while, therefore, the creditor able to establish a *prima facie* case for sequestration, is to have the benefit of preservation of the debtor's property, an opportunity is to be afforded to the debtor and all his other creditors to be heard in relation to the issue of whether a final order of sequestration should be granted."

188 Para 4.

which was confirmed on the return date.[189] In arriving at its decision to confirm the provisional order, the court held that Mr Thorpe in fact controlled the trusts. The impression is inescapable that it foresaw the possibility that the trust's assets could eventually be used to satisfy Mr Thorpe's creditors.[190]

Van der Merwe NO v Hydraberg Hydraulics CC[191] presented a further opportunity to consider the type of abuse that would merit a disregard of the trust estate. The facts were briefly as follows. A close corporation, Hydraberg Hydraulics CC ("Hydraberg CC"), and a trust, the Hydraberg Property Trust ("the property trust") sold a going concern, together with the immovable property from which it operated, to the trustees of the Monument Trust in terms of a single indivisible agreement ("the sale agreement"). A dispute between the parties ensued and at issue was the validity of this sale agreement. The respondents contended that the sale agreement was invalid for non-compliance with the joint-action rule.[192]

Clarke and Bosman, the *dramatis personae* on the part of Hydraberg CC and two of the three trustees of the property trust, effectively side-lined the third trustee, one Slabbert, from all administration of the trust and he took no part in concluding the sale agreement. Seeking to profit from this state of affairs and avoid the property trust's obligation under the sale agreement, Clarke and Bosman contended that, since they alone signed the sale agreement, the trust could not have been bound. What compounded matters was that, as soon as Slabbert was removed as trustee and another appointed in his stead, Clarke and Bosman caused a resolution to be passed by the property trust affirming that the property trust was not a party to the sale agreement and that it had not granted Clarke and Bosman authority in writing to enter into it.

This conduct on the part of Clarke and Bosman moved the court to affirm that:

> "The facts of the current matter afford a classic example of an abuse of the trust form flowing directly from the conduct of Clarke and Bosman in respect of the ownership of the fixed property, with no distinction between their responsibilities as trustees and their

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189 The final judgment is reported as *Nedbank v Thorpe* ZAKZPHC 16-09-2009 case no 7392/2007.

190 Such an order was made in respect to a different debtor in *First Rand Limited t/a First National Bank v Britz* ZAGPPHC 20-07-2011 case no 54742/09.

191 2010 5 SA 555 (WCC).

192 The "joint-action rule" is discussed in detail in Chapter 5: see part 5 4.

expectations as beneficiaries. They treat the property as their own, and invoke the existence of the trust only when it suits them."[193]

The court ultimately considered itself unable to disregard the trust estate on account of the provisions of the Alienation of Land Act 68 of 1981.[194] However, *Hydraberg* remains of significant assistance in determining the *type* of abuse that would move a court to disregard the trust estate. A hallmark of Clarke and Bosman's conduct is that they simply ignored their fiduciary duty to act independently of their own interests in managing the trust estate.

In *Van Zyl v Kaye*[195] the same court, also per Binns-Ward J, took the opportunity to further elucidate the circumstances under which the separate estate of a trust is to be disregarded.

In that matter, the applicants, who were the provisional trustees in the insolvent estate of Mr Kaye, applied for an order declaring that two immovable properties, which were held by a trust and a private company respectively, be regarded as the personal assets of Mr Kaye.[196] Against the trust, the applicants requested the court to disregard the separate trust estate in terms of its powers under the common law. As against the company, the applicants relied on the provisions of section 20(9) of the Companies Act 71 of 2008.[197]

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193 *Van der Merwe NO v Hydraberg Hydraulics CC* 2010 5 SA 555 (WCC) para 39.

194 Section 2 of that Act provides that a party entering into an agreement on behalf of another is required to have been authorised thereto in writing. See, however, the insightful discussion by Van der Linde, where he argues that mechanisms exist to obviate the above legislative difficulty on the facts of *Hydraberg*: A van der Linde "Debasement of the core idea of the trust and the need to protect third parties" (2012) 75 *THRHR* 371.

195 2014 4 SA 452 (WCC).

196 *Van Zyl NNO v Kaye NO* 2014 4 SA 452 (WCC) para 1.

197 That section codified the doctrine of piercing the corporate veil, and provides as follows: "If, on application by an interested person or in any proceedings in which a company is involved, a court finds that the incorporation of the company, any use of the company, or any act by or on behalf of the company, constitutes an unconscionable abuse of the juristic personality of the company as a separate entity, the court may-

(a) declare that the company is to be deemed not to be a juristic person in respect of any right, obligation or liability of the company or of a shareholder of the company or, in the case of a non-profit company, a member of the company, or of another person specified in the declaration; and

After emphasising the distinction between an invalid or "sham" trust on the one hand,[198] and "disregarding the separate estate" of the trust on the other, the court proceeded to coherently articulate the difficulty in formulating a general test for such relief as follows:

> "Going behind the trust form (or 'piercing its veneer', as the concept is sometimes described) essentially represents the provision by a court of an equitable remedy to a third party affected by an unconscionable abuse of the trust form. It is a remedy that will be afforded in suitable or appropriate cases … I suspect that, rather like the position with 'piercing of the corporate veil' in the case of companies, closely defining the applicable principles in the cases in which it is afforded or withheld may prove elusive. That is why I consider it appropriate to describe it as an equitable remedy in the ordinary, rather than technical, sense of the term; one that lends itself to a flexible approach to fairly and justly address the consequences of an unconscionable abuse of the trust form in given circumstances. *It is a remedy that will generally be given when the trust form is used in a dishonest or unconscionable manner to evade liability, or avoid an obligation*."[199]

This test, therefore, postulates two elements. Firstly, it is required that the trust form be used in a dishonest or unconscionable manner, and secondly, that it is used to avoid some liability or obligation. While, on the facts of that matter, the court concluded that the applicants had "not shown that the Trust was used dishonestly or unconscionably to evade liability to them or Kaye's creditors",[200] the elucidation of the test to be applied in disregarding the trust estate is to be welcomed.

In *WT v KT*,[201] the SCA again considered the basis upon which a trust estate may be disregarded in the context of divorce proceedings. That matter concerned a trust established prior to the parties' marriage in community of property.

The trust assets included the marital home and the shares of several companies established by WT in the furtherance of his business interests.[202] Faced with an

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(b) make any further order the court considers appropriate to give effect to a declaration contemplated in paragraph (a)."

For an insightful discussion regarding the above statutory power and a court's power under the common law to pierce the corporate veil, see Nel (2014) *Obiter* 570.

198 Also highlighted in part 6 2 above.

199 *Van Zyl NNO v Kaye NO* 2014 4 SA 452 (WCC) para 22 (emphasis added).

200 Para 30.

201 2015 3 SA 574 (SCA).

202 Para 11.

action for divorce, KT did not oppose the decree of divorce sought but contended that the trust's assets should be deemed to have formed part of the joint marital estate.[203] The court *a quo* ruled in her favour.

On appeal, the SCA held that in considering whether to disregard a trust estate one needed to look to the principles of corporate law:

> "As regards averments pertaining to 'looking' behind the veneer of the trust as the alter ego of WT, the legal principles in this respect have in essence been transplanted from the arena of 'piercing the corporate veil'. In the latter context courts are empowered to disregard the legal fiction of separate corporate personality in suitable or appropriate circumstances. Similarly, as Cameron JA noted in this court in *Land and Agricultural Bank of South Africa v Parker & Others*, if the trust form is 'debased', justice would dictate that the veneer of the trust be pierced in the interests of creditors. By analogous reasoning, unconscionable abuse of the trust form through fraud, dishonesty or an improper purpose will justify looking behind the trust form."[204]

In applying this principle, the court held that:

> "Significantly, the dicta of Cameron JA in *Parker*, pertaining to the importance of maintaining the functional separation between control (by trustees) and enjoyment (by beneficiaries) in family trusts, are premised upon the interest of third parties, who transacted with the trust."[205]

It thereby implied that a fiduciary responsibility would be limited to the beneficiaries and third parties who transact with the trust.[206]

Since KT was neither a beneficiary of the trust, nor a third party who transacted with the trust, the court held that she did not enjoy *locus standi* to seek the disregard of the trust estate.[207] In so doing the court elevated the existence of a fiduciary relationship between the trustees and the applicant to a pre-requisite for seeking the disregard of a trust estate. This position has been met with strong academic and judicial criticism.[208]

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203 Para 2.

204 Para 31.

205 Para 33.

206 Para 33.

207 *WT v KT* 2015 3 SA 574 (SCA) para 33.

208 See Shipley (2016) *SA Merc LJ* 508; Smith (2016) *JJS* 68.

The strongest critique of this approach was delivered two years later by the same court in *REM v VM*.[209] After discussing the above finding in *WT v KT*, the SCA held that:

> "[t]here can be no basis in logic or principle for a distinction to be drawn between legal standing to advance a claim to pierce the veil of a trust, by a third party who transacts with the trust on the one hand, and a spouse who seeks to advance a patrimonial claim, on the other. Breach by the trustee of his or her fiduciary duties in administration of the trust, is not the determining factor."[210]

That matter also related to the circumstances under which a party could seek the disregard of the trust estate. At issue was whether assets held in certain trusts were to be considered that of REM for the purposes of calculating the parties' respective accrual.

The evidence suggested that REM had failed to ensure a functional separation between control and benefit of certain trusts and indiscriminately caused trust assets to be applied for his personal benefit. Swain JA, writing for a unanimous court, endorsed the proposition by Binns-Ward J in *Van Zyl v Kaye*,[211] to the effect that disregarding the trust estate is an equitable remedy that requires either dishonesty or unconscionable use on the one hand and the evasion of some liability or obligation on the other.[212]

Against this background the court identified that:

> "The conduct of [REM] in allegedly transferring personal assets to these trusts, dealing with them as if they were assets of these trusts and not properly performing his fiduciary duties, all with the object of concealing these assets and thereby defeating the accrual claim of the respondent, are the central issues in determining whether the trust veneer should be pierced."[213]

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209 2017 3 SA 371 (SCA).

210 Para 20.

211 2014 4 SA 452 (WCC).

212 *REM v VM* 2017 3 SA 371 (SCA) para 17.

213 Para 19.

The court expressly rejected the conclusion in *WT v KT*[214] that confined standing to advance a claim for the disregard of the trust estate to those to whom the trustee owes a fiduciary duty, and held that breach "by the trustee of his or her fiduciary duties in the administration of the trust, is not the *determining factor*".[215] The court held that:

> "In either case, a claim lies against the trust, or the errant trustee, on the basis that the unconscionable abuse of the trust form by the trustee, in his or her administration of the trust, through fraud, dishonesty or an improper purpose prejudices the enforcement of the obligation owed to the third party, or a spouse. [VM] had to prove that [REM] transferred personal assets to these trusts and dealt with them as if they were assets of these trusts with *the fraudulent or dishonest* purpose of avoiding his obligation to properly account to [VM] for the accrual of his estate …"[216]

The inference is clear – the focus in considering whether to disregard the trust estate is not on the possible fiduciary breach, but on the unconscionable use of the trust form to evade some obligation.

On this basis, the court ultimately held that, notwithstanding that it appeared that REM had dealt with trust assets as his own, there was insufficient evidence to conclude that he did so for the fraudulent or dishonest purpose of avoiding his obligation to properly account for the accrual of his estate.[217] The appeal was accordingly upheld and the order *a quo* substituted.[218]

6 5 3 What type of abuse?

It is submitted that the test in *Van Zyl v Kaye*,[219] and endorsed in *REM v VM*,[220] builds on the principles of the test developed in *Cape Pacific v Lubner*.[221] This much appears from the requirement that for a party to succeed with an order disregarding the trust estate, some form of unconscionable use of the trust form is required.

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214 2015 3 SA 574 (SCA).
215 *REM v VM* 2017 3 SA 371 (SCA) para 20 (emphasis added).
216 Para 20.
217 Para 20.
218 Para 28.
219 2014 4 SA 452 (WCC).
220 2017 3 SA 371 (SCA).
221 1995 4 SA 790 (A).

This requirement has been criticised as superfluous by Cameron et al as follows:

> "However, in our view dishonesty or unconscionability should not necessarily be seen as requirements before trustee conduct can be described as trust abuse. A general disregard of the functional separation between the ownership (or control) of trust assets and its enjoyment and non-compliance with the basic principles of trust administration … could also be indicative of trust abuse under appropriate circumstances."[222]

As discussed in Chapter 2, a core element of the trust is the separation between control and benefit.[223] This element is safeguarded through the "principles of trust administration" which are in turn grounded in a trustee's fiduciary duty, including the duty of independence. In this context, the fiduciary proposition is relevant as any abuse of the trust form that would permit a disregard of the trust estate, would by necessary implication require a breach of a trustee's fiduciary duty in failing to maintain a sufficient degree of independent discretion.

This is echoed by De Waal who, after analysing *Badenhorst,*[224] *Thorpe*[225] and *Hydraberg*[226] suggests that:

> "The case analysis in the previous section, in my view, points strongly towards what may be called the 'principles of trust administration'. In South African law, these principles have been formulated as follows: (1) the trustee is bound to exercise an independent discretion; (2) the trustee must give effect to the trust deed (or instrument), properly interpreted; and (3) the trustee must, in the performance of duties and the exercise of powers, act with care, diligence and skill. Instead of referring to these 'principles', one may also call them the core 'duties' of a trustee … My submission is that the … cases where the courts have considered, or in fact decided, to go behind the trust are indeed cases where the trustees have failed in one or more of these duties."[227]

In my view, the trustee's duty to ensure the proper administration of the trust is accordingly central to any consideration of whether the trust estate is being abused.

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222 Cameron et al *Honoré* 311.

223 See part 2 4 in Chapter 2.

224 *Badenhorst v Badenhorst* 2006 2 SA 255 (SCA).

225 *Nedbank v Thorpe* [2008] JOL 22675 (N).

226 *Van der Merwe NO v Hydraberg Hydraulics CC* 2010 5 SA 555 (WCC).

227 De Waal (2012) *RabelsZ* 1095.

It is submitted that where a trustee ensures compliance with the core duties of trust administration, there is no room for such abuse.

The above begs the question: why would unconscionable abuse or dishonesty be a requirement in piercing the corporate veil, but not necessarily in the context of disregarding the trust estate?

The answer lies in the public nature of the trustee office. Where the occupation of an office is purely a private law arrangement it may be argued that it is legitimate to transcend the divide between control and benefit. For example, there can be no objection in principle against a single shareholder also being the sole director of a company. However, when that comity of interests is abused to the detriment of third parties, it invites the intervention of the courts.

In contrast, and in view of the public nature of the office of trusteeship, the blurring of the lines between control and benefit in the trust context is not permissible. Therefore, in the appropriate circumstances a court could disregard the separate trust estate where there exists a "disregard of the functional separation between the ownership (or control) of trust assets and its enjoyment and non-compliance with the basic principles of trust administration"[228] irrespective of whether an element of dishonesty accompanies such conduct.

However, even if my views in this regard are incorrect, and the approach adopted in *Van Zyl v Kaye*[229] and *REM v VM*[230] is preferred, I submit that the fiduciary proposition still has an important function to fulfil.

My submission is that the dicta in *REM v VM* that a fiduciary breach is "not the *determining* factor"[231] should not be interpreted to mean that a fiduciary breach is not a pre-requisite for a disregard of the trust's separate estate. In my view, the SCA in *REM v VM* acknowledged a fiduciary breach by a trustee as a pre-requisite for a claim to disregard the trust estate but emphasised that the determining factor is whether, in addition to such breach, the trustee acted dishonestly or fraudulently in an attempt to evade some obligation.

Stated otherwise, there is in my view no room for the unconscionable use of the trust without such use being accompanied by a breach of the trustee's fiduciary duty.

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228 Cameron et al *Honoré* 311.

229 2014 4 SA 452 (WCC).

230 2017 3 SA 371 (SCA).

231 Para 20.

This much is borne out by the following dicta in *REM v VM*:

> "The respondent had to prove that the appellant transferred personal assets to these trusts and dealt with them as if they were assets of these trusts with the fraudulent or dishonest purpose of avoiding his obligation to properly account to the respondent for the accrual of his estate and thereby evade payment of what was due to the respondent, in accordance with her accrual claim. If established, a declaration could be made that the trust assets in question are to be used to calculate the accrual of the appellant's estate, as well as satisfy any personal liability of the appellant to make payment to the respondent. Although the appellant administered the trusts with very little regard for his fiduciary duties as a trustee and without proper regard for the essential dichotomy of control and enjoyment essential to the nature of a trust, and although such conduct may have justified his removal as a trustee or the appointment by the master of an independent co-trustee in terms of s 7(2) of the Trust Property Control Act, the evidence did not prove that he transferred personal assets to these trusts and dealt with them as if they were assets of these trusts, with the fraudulent or dishonest purpose of avoiding his obligation to properly account to the respondent for the accrual of his estate."[232]

This is, however, not to suggest that, as in *WT v KT*,[233] a direct fiduciary relationship is a pre-requisite for a party to seek an order disregarding the trust estate.

As stated above, the office of trusteeship is a *quasi*-public office[234] and the core duties of trust administration form part of the bundle of fiduciary duties owed by a particular trustee to that office. Where a trustee fails in those duties, the trust is open to abuse of the sort which will permit courts to look beyond the trust estate in order to ensure equity. On this construction, any person with an interest in the trust asset (which would include a spouse in the position of KT in *WT v KT*[235]) would have standing to challenge the administration of the trust.

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232 Para 230 (emphasis added).

233 2015 3 SA 574 (SCA).

234 Cameron et al *Honoré* 207.

235 2015 3 SA 574 (SCA).

6 6 Conclusion

The separate estate of the trust provides an opportunity for abuse in much the same manner as the separate juristic personality of companies is abused. In evaluating whether a trust is so abused, a strict distinction must be drawn between a sham trust, being a trust that was never established, and the abuse of the trust's separate estate.

The establishment proposition provides a sound theoretical basis to evaluate whether a trust is a sham and is to be preferred over the "sham doctrine". The advantage of the establishment proposition is that it evaluates the intention of the founder in establishing a trust, which is a distinct requirement for its establishment. In this manner, the complication surrounding the common intention requirement in evaluating the obligation establishing the trust is avoided. In addition, the establishment proposition advances an objective criterion against which the type and measure of control that is to be afforded to trustees are judged.

The fiduciary proposition also provides the background against which issues of the abuse of a trust may be considered. In matters in which a trust's separate estate is abused, it is self-evident that the trustees have failed to comply with their obligations of independence in managing the trust estate.

However, whether such an abuse merits a disregard of the trust estate is a separate enquiry. In this regard, it is submitted that the test laid down in *Van Zyl v Kaye* provides valuable insights that merit further analysis and research.

CHAPTER 7: CONCLUSION

7 1 Introduction

The trust was developed to satisfy a particular societal need,[1] namely to protect the "weak and safeguard the interests of those who are absent".[2] The result was an institution where the founder would place confidence in a trustee to manage assets on behalf of another. This "confidence reposed" in trustees, as highlighted by Garton,[3] is meaningless where the trustees do not have the *capacity* to act independently and according to their own judgement and is betrayed where the trustees *fail to exercise* their capacity for independence. It is, therefore, not surprising that there is a general consensus that trustees are required to act independently.[4]

However, the debate surrounding the theoretical basis for this principle has given rise to two, seemingly contradictory, propositions.[5] There are some who view trustee independence as a pre-requisite for the establishment of the trust, identified herein as "the establishment proposition",[6] and others who contend that it is merely a facet of a trustee's fiduciary duty, identified herein as the "fiduciary proposition".[7]

I have argued that these two propositions are not contradictory at all but, in fact, complementary. This argument was advanced through what has been identified as the "independence duality model" in which the capacity for independence by trustees is a key element of the establishment of a trust and, once established, gives rise to a fiduciary duty to exercise such independent capacity.[8]

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1 See part 2 2 2 in Chapter 2.

2 T Honoré "Trusts" in R Zimmerman & D Visser (eds) *Southern Cross: Civil Law and Common Law in South Africa* (1996) 849, endorsed in *Land and Agricultural Bank of South Africa v Parker* 2005 2 SA 77 (SCA) para 19.

3 J Garton *Moffat's Trust Law* 6 ed (2015) 1. See the text to n 1 in Chapter 1.

4 *PPWAWU National Provident Fund v Chemical, Energy, Paper, Printing, Wood and Allied Worker's Union* 2008 2 SA 351 (W); *Afrisure CC v Watson NO* 2009 2 SA 127 (SCA); MJ de Waal "The liability of co-trustees for breach of trust" (1999) 10 *Stell LR* 32; F du Toit "A trustee's duty of independence" (2009) 72 *THRHR* 637.

5 See part 3 3 in Chapter 3.

6 See part 3 3 1 in Chapter 3 and the discussion as a whole in Chapter 4.

7 See part 3 3 2 in Chapter 3 and the discussion as a whole in Chapter 5.

8 See part 3 4 in Chapter 3.

Chapter 1 identified seven practical examples that illustrate the utility of the independence duality model and its constituent parts of the establishment and fiduciary propositions. In this concluding chapter, I will revisit these examples, drawing from the analysis of the establishment and fiduciary propositions in the preceding chapters.

7 2 The independence duality model

The perception that the establishment and fiduciary propositions are mutually exclusive[9] is attributable to a failure to recognise a duality in the broader concept of trustee independence.

The recognition of this duality enables a reconciliation of the establishment and fiduciary propositions and reveals that each of these propositions offers a sound theoretical basis for one distinct component of trustee independence.

Before it can be said that a trustee acts independently, two elements must be present. First, the trustee must be afforded the *capacity* to act independently and, secondly, the trustee must thereafter *exercise* this capacity. Where the first factor is absent, a "trustee" cannot be said to be acting independently and, where notwithstanding this capacity for independence, a trustee nevertheless fails to act in an independent manner, it can similarly not be said that the trust benefits from independent administration by the trustee.

The proposition is accordingly advanced that, on both a theoretical and a practical level, there is a duality in the concept of "trustee independence", namely, the *capacity* for independent administration being afforded to the trustees, and the *exercise* of that capacity. This, in essence, constitutes the "independence duality model".[10]

These two factors are entirely distinct but connected to the broader principle of trustee independence and the establishment and fiduciary propositions relate to only one aspect in turn. The distinct nature of each of these two elements means that the test in respect of establishing the presence of each is also distinct.

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9 See part 3 2 in Chapter 3.

10 See part 3 4 in Chapter 3.

The establishment proposition serves to explain the capacity for independence and the fiduciary proposition relates to the question of the exercise of such independence.

The establishment proposition requires an objective evaluation of whether the trustee is afforded the capacity for independence at the time of the trust's establishment. In contrast, the fiduciary proposition requires an evaluation of the manner in which the trustee had exercised this capacity. It follows that this requires a factual analysis on a case by case basis.[11]

It is against this background that the establishment and fiduciary propositions can, and should, be reconciled and it is argued in this dissertation that it is incorrect to label these two propositions as mutually exclusive or otherwise incompatible.[12]

As long as the trustees are afforded the capacity for independent administration of the trust, it does not matter (in the context of the establishment proposition) that there are risks that they may fail to exercise this capacity independently. Once such capacity is established, the establishment proposition holds that a valid trust is established (on condition that the other requirements for a trust are present). Then questions regarding the failure of the trustees to act independently shift to be determined with reference to the principles underlying the fiduciary proposition.

7 2 1 The establishment proposition

It has been argued in this dissertation that, while trustee independence is not generally recognised as a requirement for the establishment of a trust,[13] it does form part of the *essentialia* of the trust institution.[14]

As the discussion on the historical development of the trust institution has shown, the trust developed from a need to entrust control over the management of assets to

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11 See part 3 4 in Chapter 3.

12 See part 3 4 1 in Chapter 3.

13 The recognised requirements to establish a valid trust are:
(i) an intention on the part of the founder to create a trust;
(ii) the expression by the founder of the intention to create a trust in a mode suited to the creation of a legal obligation;
(iii) a reasonably certain definition of the trust property;
(iv) a reasonably certain definition of the trust object; and
(v) the lawfulness of the trust object.

14 See part 3 4 1 in Chapter 3.

another, who was required to assert such control not in their own interest but in that of a third party.[15] Where this vesting of control in the hands of the trustee is not present, in the sense that the trustee is not free to exercise independent control, it has been argued that no trust is established because the divestment of control in favour of the trustee is an indispensable characteristic of the trust.

Accordingly, independent control may be (indirectly) incorporated into the requirements for the establishment of a trust, as it is an indispensable element of the *definition* (and, indeed the *conception*) of a trust.[16]

The type of control required in the context of a trust is *asset* control. In other words, it is imperative that the trustees have control over the manner in which the trust assets are employed. While *structural* control,[17] being the power to amend the structure of the trust, such as dismissing trustees, held by another may invite manipulation of the manner in which the trustees exercise their asset control, structural control is not relevant for the purposes of the establishment proposition.[18]

This is because, in view of the independence duality model, trustees have a fiduciary duty to exercise independent control over the administration of the trust, once a trust is established and they are, by implication, vested with independent asset control.[19] For the purposes of determining whether a trust has been established, it is irrelevant whether a trustee may in future submit to manipulation on the basis of incentives or threats wielded by others, the consequences of which are to be considered through the lens of the fiduciary proposition.[20]

The measure of asset control to be afforded the trustees in terms of the establishment proposition is absolute in the sense that it should be the body of trustees alone that has the power to employ the trust assets. This, however, does not mean that the trustees' discretion cannot be curtailed through the trust deed. Due to the nature of trusteeship, being a *quasi*-public office, it is permissible for a founder to put assets in trust, but simultaneously to restrict the trustees' discretion to employ

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15 See part 2 2 in Chapter 2.

16 See part 3 4 1 in Chapter 3.

17 For a discussion on the distinction between asset control and structural control, see part 4 2 in Chapter 4.

18 See part 4 5 in Chapter 4.

19 See part 3 3 1 in Chapter 3.

20 See part 5 3 in Chapter 5.

the trust assets.[21] This restriction does not translate to the curtailment of asset control because it still vests in the trustees alone. It is only the powers of the trustees in relation thereto that are restricted.

Such a restriction is possible precisely due to the nature of trusteeship as an office with powers flowing from the provisions of the trust deed.[22]

7 2 2 The fiduciary proposition

The fiduciary proposition holds that, once a trust has been established, the trustees occupying the office of trusteeship are duty-bound to exercise independent discretion in the exercise of their powers.[23] This obligation stems from a trustee's occupation of the office of trusteeship and forms part of a trustee's fiduciary duty.

Unlike the establishment proposition, the fiduciary proposition is concerned with the *manner* in which the trustees exercise their obligation of independence as opposed to *whether* they are afforded such capacity. It follows that the fiduciary proposition focuses on the conduct of the trustees throughout the existence of the trustee office.

This characteristic accounts for the explanation of what has been described as "developing non-independence" in a manner that the establishment proposition is unable to do.

The fiduciary proposition emphasises a trustee's duty of independence as part of the fiduciary duty that flows from the office of trusteeship. It is contended herein that, as a consequence, a general disregard for the separation of control and benefit, that is central to the trust idea, amounts to sufficient dereliction of duty to qualify as an abuse that justifies a court to disregard the separate estate of the trustee (or "separate trust estate" as it is referred to for the sake of convenience in this dissertation).[24]

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21 See part 4 6 in Chapter 4.

22 For a discussion of trusteeship as an office, see part 2 4 4 in Chapter 2.

23 See part 3 3 2 in Chapter 3.

24 See part 6 2 and part 6 5 3 in Chapter 6.

7 3 Application of the theoretical framework to examples

The examples identified in Chapter 1 serve to illustrate the practical application of the independence duality model and its two constituent parts, the establishment and fiduciary propositions. They relate primarily to questions regarding whether a trust is established (or in the alternative constitutes a so-called "sham")[25] and whether the conduct described therein amounts to abuse that may merit a court disregarding the separate trust estate.

For ease of reference, the examples are reproduced below.

7 3 1 Example 1

> Assume an *inter vivos* trust where the founder does not intend to relinquish full control over the trust assets. To achieve this end, he establishes a trust for the benefit of his children with three independent trustees and provides them with wide discretionary powers. However, he includes a provision in the trust deed to the effect that all decisions by the trustees are to be approved by the founder in order to be effective.
>
> What is the effect of this provision and does this arrangement qualify as trust?

In this example, no trust is established. The impediments to the establishment of a trust are two-fold. First, and on a subjective level, the founder does not intend to establish a *trust*. As the discussion of the requirements for validity of a trust revealed,[26] the divestment of control in favour of the trustees is an essential dimension of the definition of a trust. Accordingly, and notwithstanding the subjective understanding of the founder, where he intends to establish an arrangement in which control over the assets is retained, that arrangement cannot qualify as a trust.

Secondly, the founder also fails, objectively, to establish a trust on account of retaining asset control over the employment of the trust assets.[27] Notwithstanding that the trustees are empowered with wide "discretionary powers", these powers are qualified by making them subject to the approval of the founder.

In so doing, the founder has failed to divest himself of control over the trust assets. The discretion afforded to the trustees is rendered nugatory through the obligation that all trustee decisions are to be approved by the founder. In this sense,

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25 For criticism on this terminology see part 6 3 in Chapter 6.

26 See part 3 4 1 in Chapter 3.

27 See part 6 5 3 in Chapter 6.

the example mirrors the facts of *Humansdorp Co-operative Ltd v Wait*[28] ("*Wait*"). In *Wait*, the founder was also a trustee where the trust deed provided that trustee decisions were to be taken by way of majority vote. Significantly however, it was an additional requirement that the founder forms part of the majority in each instance. It followed that valid decisions by the body of trustees would always have required the concurrence of the founder.

The position would have been different if the trust deed provided that decisions were only to be taken unanimously. In such an instance, full asset control would vest in the body of trustees and it would not matter that the founder was also a trustee. The consequence would be that, should the founder no longer qualify as trustee for any reason, his influence in trustee decisions would similarly cease.

However, in the example above, the trustees' decisions are made conditional upon the approval of a person who is not a trustee and, accordingly, it cannot be said that the trustees have sufficient asset control for the arrangement to qualify as a trust.

7 3 2 Example 2

These examples examine the impact of an over prescriptive trust deed on the one hand and a trust deed that affords the founder particularly far-reaching structural power on the other, within an otherwise identical factual matrix. This small distinction has significant consequences. Hence the example is divided into two examples, example 2a and example 2b.

7 3 2 1 Example 2a

> The founder establishes an *inter vivos* investment trust. The trust deed contains detailed and prescriptive provisions to the trustees. They are to invest the trust assets only in shares identified in an annexure to the trust deed, and only in the ratio set out therein.
>
> The trust deed further requires that all proceeds from the investments be immediately re-invested in the same shares (and in accordance with the same ratio). It is expressly recorded that the trustees have no discretion in the investment of the trust assets and no amendment of the trust deed is permitted.

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[28] Case no 2896/2012, Eastern Cape Division of the High Court, Grahamstown, (now Mkhanda) delivered on 1 November 2016. For a discussion of this case see part 6 4 2 in Chapter 6.

> On the twenty-first anniversary of the trust, the trustees are to immediately liquidate the trust assets, pay the proceeds to the founder's surviving issue *per stirpes* and terminate the trust.
>
> There is accordingly no requirement that the decisions of the trustees be approved by the founder but the trustees' powers and duties are prescriptive in nature, with no discretion on their part. Does this arrangement qualify as a trust?

In this example, the founder retains significant, albeit indirect, control through the prescriptive trust deed. However, in contrast to example 1, the arrangement in this example *does* constitute a trust. This is because, notwithstanding the curtailment of the trustees' discretion, full asset control still vests in them.[29]

Unlike in example 1, the founder does not have the power, once the trust has been established, to determine the manner in which the assets are to be employed. Full asset control vests with the body of trustees with only the exercise thereof limited by the trust deed. The *quasi*-public nature of trusteeship as an office, therefore provides the theoretical framework that permits a trust such as in this example.

Once the assets are donated into trust, they are sequestered from the founder's estate, thereby establishing the trust estate. The trust deed regulates the powers of the trustees (and the trustees remain subject to supervision by the courts and the Master).

It does not matter that the founder may prescribe the manner in which the trustees are to deal with the trust assets as he is divested from any further control after the establishment of the trust. The significant distinction lies therein that any "control" that the founder may exercise in the establishment of the trust, ceases once the trust is established. At this point in time the founder no longer has any control to dictate the manner in which the trust assets are administered.

This example accurately illustrates the versatility of the trust institution as there is no legal objection to the founder employing the trust deed to determine the manner in which assets are to be dealt with after having relinquished control.

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[29] See part 4 4 5 in Chapter 4.

7 3 2 2 Example 2b

> This example is identical to example 2a, with the only distinction being that the founder retains the power to amend the trust deed and, accordingly, the power of investment of the trustees.

In example 2b, no trust is established. The example may initially seem complex because it appears that asset control remains in the hands of the trustees and that only structural control is vested in the founder.

However, while the power to amend the trust deed may appear to be structural in nature, it qualifies as asset control when such power may be used to *compel*, as opposed to influence, the trustees to act in a certain manner.

Accordingly, were the founder to use such power to amend the manner in which the trust assets were to be applied, this would render the “asset control” enjoyed by the trustees nugatory and, as a consequence, no valid trust would be established.

It is accordingly clear that asset control may also be disguised as structural control.

7 3 3 Example 3

> A founder establishes an *inter vivos* trust and appoints three independent trustees. The trustees are granted absolute discretion to invest the trust assets as they wish, to pay the income from the investments to nominated income beneficiaries and, upon their death, to allocate the balance to nominated capital beneficiaries.
>
> To assist the trustees, the founder furnishes them with a letter of wishes proposing the manner of investments to be undertaken. The letter expressly records that the trustees are not bound by its content.
>
> However, the trust deed contains a provision to the effect that the trustees’ remuneration is to be determined by the founder on an annual basis, and that the founder may dismiss a trustee in writing.
>
> During the currency of the trust, the founder regularly determines the trustees’ annual remuneration in accordance with how closely they followed the suggestions in the letter of wishes. On one occasion, and following from the trustees’ refusal to follow any of the proposals in the letter of wishes, the founder dismisses the entire board of trustees and replaces them with three other persons.
>
> Can it be said that this arrangement qualifies as a trust?

This example differs from example 2a in that the trustees are afforded full discretion in the manner in which the trust assets are to be employed. Significantly,

the trustees have full asset control over the trust assets thereby, and in accordance with the establishment proposition, establishing a trust.

However, the measure of structural control retained by the founder is significant. As discussed in Chapter 4, structural control may be employed to manipulate trustees to do as a founder suggests.[30] This may be achieved through what has been described as the "*in terrorem*" quality of the structural control retained.[31]

In this example, the founder has summarily dismissed recalcitrant trustees and rewarded trustees who have adopted his suggestions. However, while a sound argument may be made that such conduct compromises the independence of the trustees, it does not compromise the validity of the trust.

This is so because, in terms of the establishment proposition, a trust will be established when, at the time of its establishment, the trustees are afforded full asset control.

The trustees' fiduciary duty requires that they exercise such asset control independently, notwithstanding the *in terrorem* quality of the structural control retained by the founder.

However, when "structural control" enables a founder to dictate or influence the manner in which the trust assets are employed, such as in example 2b, the control no longer relies on its *in terrorem* quality, but its innate capacity to control the assets of the trust. Such control would therefore also qualify as asset control and result therein that no trust is established.

7 3 4 Example 4

> A founder, a successful commercial farmer, donates the family farm and farming enterprise to a trust. He appoints five trustees, including himself, his wife, two sons and his accountant. The trustees are afforded unlimited discretion in the management of the trust assets and the beneficiaries are the founder and his family.
>
> From the outset it is clear that the other trustees never question the management of the trust by the founder. Where resolutions are required, they all submit to his will in habitual deference and never bring an independent mind to bear upon the administration of the trust.
>
> Does the conduct of the trustees imperil the existence of the trust?

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30 See part 4 5 in Chapter 4.

31 RDM Flannigan "The control test of principal status applied to business trusts: Part II" (1986) 8 *Est & Tr Q* 97 113.

In this example, the trustees' conduct does not imperil the existence of the trust. It is clear that the trustees are afforded sufficient capacity for independence to meet the requirements of the establishment proposition and, provided all other requirements were met, there can be no objection to the validity of the trust. However, the trustees' failure to bring an independent mind to bear upon the administration of the trust may provide the basis to hold them personally liable for any loss suffered by the beneficiaries. As discussed in Chapter 5,[32] in *Wiid v Wiid* ("*Wiid*")[33] trustees were held liable to the beneficiaries for breach of trust on this basis.

Stated otherwise, the basis on which the trustees may be held liable for any loss suffered by the beneficiaries is breach of their fiduciary duty. This duty flows from the office of trusteeship because it is as a result of the trustees occupying that office that they are required to bring an independent mind to bear on the administration of the trust.[34]

7 3 5 Example 5

> Consider the following alternative. The facts are identical to those of example 4, except that the trustees *do* bring an independent mind to bear upon the administration of the trust. At first, the trustees engage in robust debate surrounding the management of the trust assets and the enterprise as a whole, arriving at a decision (not always by consensus). With the passing of time, the founder's eldest son starts to play an increasingly prominent role in the management of the trust estate.
>
> In time, the position develops where the remaining trustees simply permit the eldest son to manage the farm and farming enterprise as he sees fit and the remaining trustees come to simply submit to the will of the eldest son in habitual deference.
>
> What is the effect of this gradual deterioration of trustee independence?

The acknowledgement of the independence duality, and the acceptance of the establishment and fiduciary propositions, allow for an explanation of the

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32 See part 5 3 in Chapter 5.

33 NCHC 13-01-2012 case no 1571/2012.

34 See the discussion of *Griessel NO v De Kock* 2019 5 SA 396 (SCA) in part 5 3 in Chapter 5, where it is emphasised that a trustee's fiduciary duty is rooted in their occupation of the office of trusteeship.

phenomenon of “developing non-independence”.[35] In the above example, the trustees are afforded the *capacity* for independence within the framework of the establishment proposition. Initially, the trustees also *exercise* this capacity in accordance with their fiduciary obligation to do so.

The establishment proposition is unable to provide a theoretical basis for the consequences that follow in the event of developing non-independence. Once a trust is validly established it is intellectually incoherent to suggest that this validity may be compromised on account of trustees failing to act with the required independence.

Since the establishment proposition requires an objective assessment at the time that the trust is established, it plays no role in determining the consequences of the developing non-independence highlighted above. In contrast, this phenomenon may be easily explained if it is accepted that there is a duality in trustee independence and that the exercise of the capacity for independence is regulated through the fiduciary proposition. Once it is accepted that trustees have a fiduciary duty to bring an independent mind to bear upon the administration of the trust, it is irrelevant whether a breach of this duty occurs at the commencement of the trust or later.

In accordance with this proposition, the trustees’ failure to properly exercise independent discretion in the administration of the trust does not imperil the validity of the trust but, as in the previous example, exposes the trustees to a claim for breach of trust. The phenomenon of developing non-independence accordingly underscores the utility of the independence duality model and its constituent, and complimentary, parts.

7 3 6 Example 6

> A founder establishes a trust with the stated purpose of conducting a second-hand car sale business. The trustees are the founder, his business partner and an independent accountant. The trust deed requires that all the trustees act jointly in the administration of the trust. However, in reality, the accountant is never involved in the administration of the trust and the remaining trustees conduct the business without any reference to him. Effectively he is side-lined.
>
> At one occasion the two trustees, purporting to act on behalf of the trust, enter into a sale agreement of all available trust stock with a third party. When market conditions change prior to delivery, it is apparent that the trust could sell the stock to another party at a premium. In order to profit from this state of affairs, the two trustees refuse to honour

[35] See part 3 4 5 in Chapter 3.

the first sale agreement, invoking in their defence that the third trustee was not a party thereto, rendering the sale agreement void.

What remedy, if any, does the third party to the first sale agreement have?

Examples 6 and 7 relate to the circumstances under which a court may be invited to disregard the separate estate of the trust. As discussed in Chapter 6, this power is rooted in the common law[36] and stems from the duty of the courts to develop the trust law.[37]

Example 6 is based on the factual matrix of *Van der Merwe NO v Hydraberg Hydraulics CC* ("*Hydraberg Hydraulics*"),[38] save that the object of the sale is movable property as opposed to immovable property.[39] The salient features are that the founder and business partner ("the trustees") did not ensure a functional separation (and hence independence) between their private interests and their obligations as trustees. In addition, the trustees in question seized upon an opportunity to resile from the sale agreement on account of their own fiduciary breach.

On the basis of the test set out in *Van Zyl v Kaye*,[40] and endorsed in *REM v VM*,[41] the third party would be able to hold the trustees personally liable for the breach of the sale agreement if it could prove that (i) the trust form was used in a dishonest or unconscionable manner and (ii) in order to avoid some liability.[42]

On the facts of example 6, this test would be met. The trustees used the trust in a dishonest manner by failing to distinguish between their private interest and their obligation as trustees and subsequently capitalised on this dereliction of duty to avoid a contractual liability.

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36 *RP v DP* 2014 6 SA 243 (ECP) para 31.

37 See part 6 5 1 in Chapter 6.

38 2010 5 SA 555 (WCC). For a discussion of this case see part 6 5 2 in Chapter 6.

39 This is in order to obviate any debate surrounding the application (if any) of the Alienation of Land Act 68 of 1981. In *Hydraberg Hydraulics*, the court considered itself constrained by section 2 of that Act. That section provides that a party entering into an agreement for the sale of immovable property on behalf of another is required to have been authorised thereto in writing. There is however debate surrounding whether the court was bound in this manner. See A van der Linde "Debasement of the core idea of the trust and the need to protect third parties" (2012) 75 *THRHR* 371.

40 2014 4 SA 452 (WCC).

41 2017 3 SA 371 (SCA).

42 See part 6 2 5 in Chapter 6.

This is accordingly a suitable example where the third-party purchaser may request the court to disregard the separate estate of the trust and hold the trustees personally liable for the breach of contract.

7 3 7 Example 7

> A founder establishes various trusts to house his business, property portfolio, and investments. He is also the sole trustee and his children are the beneficiaries. He fails to ensure any functional separation between the various trusts and expenses are often shared. The maintenance of himself and his family is funded through the various trusts.
>
> Long after the establishment of the trusts, the founder commences a business venture in his personal capacity. Upon the failure of this business venture, his personal creditors seek to execute against the trusts.
>
> Would these creditors enjoy any prospect of success?

This example is based on the facts of *REM v VM*.[43] The primary distinction between this example and example 6 lies therein that the conduct in example 6 may be described as "dishonest" or "unconscionable" whereas the founder in example 7 did not *prima facie* act in such a manner. Therefore, were the test set out in in *Van Zyl v Kaye*,[44] and endorsed in *REM v VM*,[45] be applied to this example, it is unlikely that a court would accept the invitation to disregard the trust's separate estate.

The question, however, arises whether, in these circumstances, where dishonesty or unconscionability is not apparent, the failure by the trustee to ensure a functional separation between control and benefit of the trust may nevertheless justify a finding disregarding the separate trust estate. It has been argued herein that it could.[46]

As a result of the *quasi*-public nature of the office of trusteeship, it is submitted that the conflation of interests and a failure by the trustee to maintain independence constitutes sufficient abuse of the trust form to warrant disregarding the separate estate of the trust. It is precisely this public, as opposed to private, nature of the trust

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43 2017 3 SA 371 (SCA). For a discussion of this case, see the text to n 208 in part 6 5 2 in Chapter 6.

44 2014 4 SA 452 (WCC).

45 2017 3 SA 371 (SCA).

46 See the discussion at part 6 5 3 in Chapter 6.

that places the trust form on a different footing to juristic persons such as companies.[47]

Applying this approach, rooted in the fiduciary proposition, the creditors would, in my view, enjoy some prospect of success in executing against the various trust estates on account of their abuse.

7 4 Conclusion

The trust developed organically as a result of a human need to ensure the protection of those who would otherwise be vulnerable.[48] Central to the trust form is the confidence placed in the character of the trustee to execute his obligations with care, diligence and skill, and to do so independently.

The two principal propositions for a trustee's obligation of independence are complimentary: explaining, on the one hand, why a trust would fail for want of independence and also, on the other hand, determining the consequences of the failure on the part of the trustee who disregards this duty.

Through the lens of the independence duality model, its two constituent parts, the establishment and fiduciary propositions, may be reconciled. This provides a sound theoretical basis also to determine questions of sham trusts and abuse of the trust form.

It is accordingly submitted that the recognition of the independence duality model would represent a significant development in both understanding the theoretical underpinnings of the South African trust and in dealing with practical problems related to the validity and the abuse of trusts.

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47 See part 6 5 3 in Chapter 6.

48 See part 2 2 in Chapter 2.

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